S. Hrg. 100-309

THE TRUTH IN SAVINGS ACT

HEARING

BEFORE THE

SUBCOMMITTEE ON CONSUMER AFFAIRS

OF THE

COMMITTEE ON
BANKING, HOUSING, AND URBAN AFFAIRS
UNITED STATES SENATE

ONE HUNDREDTH CONGRESS

FIRST SESSION

ON

S. 1507

TO PROVIDE FOR THE UNIFORM DISCLOSURE OF THE RATES OF INTEREST WHICH ARE PAYABLE ON SAVINGS ACCOUNTS, AND FOR OTHER PURPOSES

AUGUST 5, 1987

Printed for the use of the Committee on Banking, Housing, and Urban Affairs

U.S. GOVERNMENT PRINTING OFFICE
78-039 WASHINGTON : 1987

For sale by the Superintendent of Documents, Congressional Sales Office
U.S. Government Printing Office, Washington, DC 20402

5241-10

COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS

WILLIAM PROXMIRE, Wisconsin, *Chairman*

ALAN CRANSTON, California
DONALD W. RIEGLE, JR., Michigan
PAUL S. SARBANES, Maryland
CHRISTOPHER J. DODD, Connecticut
ALAN J. DIXON, Illinois
JIM SASSER, Tennessee
TERRY SANFORD, North Carolina
RICHARD SHELBY, Alabama
BOB GRAHAM, Florida
TIMOTHY E. WIRTH, Colorado

JAKE GARN, Utah
JOHN HEINZ, Pennsylvania
WILLIAM L. ARMSTRONG, Colorado
ALFONSE M. D'AMATO, New York
CHIC HECHT, Nevada
PHIL GRAMM, Texas
CHRISTOPHER S. BOND, Missouri
JOHN H. CHAFEE, Rhode Island
DAVID K. KARNES, Nebraska

KENNETH A. MCLEAN, *Staff Director*
LAMAR SMITH, *Republican Staff Director and Economist*

SUBCOMMITTEE ON CONSUMER AFFAIRS

CHRISTOPHER J. DODD, Connecticut, *Chairman*

WILLIAM PROXMIRE, Wisconsin
BOB GRAHAM, Florida
TIMOTHY E. WIRTH, Colorado

PHIL GRAMM, Texas
JOHN H. CHAFEE, Rhode Island
DAVID K. KARNES, Nebraska

PETER KINZLER, *Staff Director*

CONTENTS

WEDNESDAY, AUGUST 5, 1987

Page
- Opening statement of Senator Proxmire ... 1
- Opening statement of Senator Dodd ... 2
- Opening statements of:
  - Senator Wirth ... 6
  - Senator Chafee ... 8
  - Senator Heinz ... 9
- Proposed bill, S. 1507 ... 10

WITNESSES

- Howard B. Brown, Commissioner of Banking, the State of Connecticut ... 22
  - Providing schedule of interest rates ... 22
  - Savers have many choices of services ... 23
  - Prepared statement ... 24
    - Deposit Account Contract Act ... 26
- Witness discussion:
  - Protection from misleading information ... 29
  - Method of notifying violators ... 31
- Theo Pitt, Jr., Vice Chairman, United States League of Savings Institutions ... 32
  - Prepared statement ... 35
- Alan Fox, Legislative Representative, Consumer Federation of America ... 39
  - Bank and thrift account fees ... 39
  - Analyzing deposit accounts ... 40
  - Prepared statement ... 41
    - Information needed for market to function ... 41
    - Comparing consumer account ... 42
    - Two parts to adequate account disclosure ... 42
    - Income disclosure ... 42
    - The need for a standardized balance calculation method ... 42
    - "Investable Balance:" Banks' version of shortweighting ... 43
    - Fees disclosure ... 44
    - The account schedule ... 44
    - Contents of the account schedule ... 45
    - Advertisements ... 45
    - Consistency of content and format ... 45
    - Mutual funds ... 46
    - Conclusion ... 47
    - List of attachments
      1. Consumer Reports chart showing effect of different balance methods on interest payments ... 48
      2. Citibank (New York State) brochure that fails to disclose fees for failure to maintain minimum balance ... 49
      3. Bank of America brochure with no information on fees ... 51
      4. Columbia First Federal Savings & Loan brochure that fails to mention balance requirement and fee for savings account ... 53
      5. American Security Bank brochure that fails to disclose money market account minimum balance requirement and fee ... 55
      6. Excerpt from First Interstate Bank of Oregon brochure stating that fee and service charge information will be provided when an account is opened ... 56
      7. Mutual Fund advertisements from the July 1987 Money ... 57

Alan Fox, Legislative Representative, Consumer Federation of America—Continued
  Prepared statement—Continued
    List of attachments—Continued — Page
      8. Letter to customers from First of America Bank mentioning, but not describing, initiation of "investable balance" method. 58
      9. June 3, 1987, letter from Alan Fox to Comptroller of the Currency Robert L. Clarke concerning "investable balance"... 59
      10. July 24, 1987, letter from Comptroller Clarke 60
Jack Shipman, Executive Vice President, Liberty National Bank and Trust Co., Louisville, KY, representing the American Bankers Association 61
  Major segments of S. 1507 questioned 61
  Competition for savings 62
  Prepared statement 64
    The electronic media 68
    Misleading description of free or no-cost accounts prohibited 68
    Schedule of fees 69
    Calculation on full amount of principal 69
    State law 69
    Conclusion 70
David Silver, President, Investment Company Institute 73
  Proposed amendments to S. 1507 73
  Example of SEC rule amendments 73
  Prepared statement 75
    I.—Introduction 75
    II.—SEC regulation of mutual fund advertising 75
    III.—Regulation of bank advertising is sorely lacking 77
    IV.—The proposed legislation represents a good beginning 78
Panel discussion:
  Method of balance calculation 87
  Variable interest rates becoming trickier 96
  Investable balance approach 96
  Fee schedules 98
  Electronic media advertising 99
Dan Goelzer, General Counsel, Securities and Exchange Commission 101
  Prepared statement 104
    I.—The regulatory scheme for investment company advertising 104
    II.—Functional differences between securities of investment companies and deposit accounts of institutions 108
    III.—Conclusion 109
Panel discussion:
  Comparing S. 1507 with existing SEC regulations 110
  Rule making process 111

ADDITIONAL MATERIAL SUPPLIED FOR THE RECORD

Prepared statement of Richard H. Lehman, U.S. Representative in Congress from the State of California 116
United States League of Savings Institutions, comments on proposed legislation 119
National Association of Federal Credit Unions, comments, on proposed legislation from Robert A. Hess, Chairman 121

THE TRUTH IN SAVINGS ACT

WEDNESDAY, AUGUST 5, 1987

U.S. SENATE,
COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS,
SUBCOMMITTEE ON CONSUMER AFFAIRS,
Washington, DC.

The subcommittee met at 2:07 p.m., pursuant to notice, in room SD-538, Dirksen Senate Office Building, Senator Christopher Dodd (chairman of the subcommittee) presiding.

Present: Senators Dodd, Proxmire, Wirth, Chafee, and Karnes.

OPENING STATEMENT OF SENATOR PROXMIRE

Senator PROXMIRE. The subcommittee will come to order.

Senator Dodd has been detained, unfortunately, in the Capitol. He will be there a little while longer, maybe for another 10 minutes or so. It's a meeting of the Democratic Party and they are discussing the Nicaraguan situation, and of course Senator Dodd is our leading expert in that area so he can't be here.

I have to be in the Capitol at 2 o'clock. So I'm going to be a little late. But I'm going to open the meeting and offer an opening statement and then recess until Senator Dodd appears, which should be very shortly after that.

I want to commend Senator Dodd for holding these hearings today on legislation which is clearly warranted. S. 1507, the Truth in Savings Act is designed to provide for the uniform disclosure of the rate of interest payable on savings accounts and the disclosure of the fees that are assessable against deposit accounts.

Ultimately the purpose of these hearings is to see what can be done to provide consumers with greater information in regard to deposit accounts.

In this regard we shall also be taking a look at mutual funds which provide similar accounts which, in my view, would be greatly helped if we could apply this legislation to it.

While the deregulation of the early 1980's has increased competition, it has also created confusion. Consumers lack the basic information they need to make prudent choices. In order for the process of deregulation to improve the efficiency of the financial marketplace through enhanced competition, it requires informed consumers who can act rationally.

Therefore, there is a critical need for the availability of accurate, complete, up-to-date and uniform information. S. 1507 is designed to meet this need so the consumers will have the ability to shop around and compare terms and conditions on which interest is paid and fees are assessed in connection with such accounts.

So I commend Senator Dodd for moving promptly on this important legislation, and I look forward to hearing from the witnesses. I wish I could be here today. I'm going to, as I say, have to run and come back, but I'll certainly carefully study the testimony in the record.

The committee will stand in recess for the next few minutes until Senator Dodd appears.

[Recess from 2:10 p.m. to 2:30 p.m.]

OPENING STATEMENT OF SENATOR DODD

Senator DODD. The Subcommittee on Consumer Affairs will come to order.

I want to apologize to all of you here this afternoon for being delayed a half an hour in starting these hearings, but we had a Democratic conference on other matters and I was unavoidably delayed as one of the principals in those discussions. So I apologize to our witnesses and others, my colleagues who may have come and could not be with us or could not stay this long.

Today the subcommittee will continue its examination of the impact of banking deregulation on consumers.

In April many of you will recall we saw how credit card issuers free from the constraints of interest rate ceilings were advertising just about everything except the cost of using a credit card.

We examined several possible solutions, including disclosure of all relevant costs at the time of solicitation and indexed rate ceilings, and I expect that the full Banking Committee will consider legislation to enhance competition this coming September.

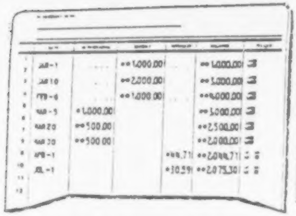
Our hearing today, however, addresses the fall-out of the deregulation of the interest rate banks can pay on consumer accounts that we began in 1980. This freedom has resulted in the availability of higher returns for depositors.

However, with this freedom has come a mind numbing variety of terms and conditions that affect actual returns, and they have not always been adequately disclosed.

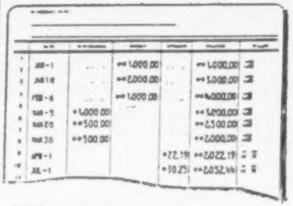
For example, the two charts that we have before us here show the importance of the method that is used to calculate the balance to which interest is applied. They reveal that the same interest rates can produce returns on the same balances that vary from $44.93 to $75.30, depending of course on whether one uses a low-balance method or a day-of-deposit to day-of-withdrawal method. Moreover, in order to properly evaluate real returns it is necessary to know what other conditions apply to the account.

Our other chart shows an August 3, 1987 advertisement from Perpetual Saving Bank for an "interest free," and I quote that checking account. What the advertisement does not tell the potential customer is that it is not possible to secure such a account unless you maintain a balance of $2,500 in that account. The missing condition is critical to the consumer's decision. Yet nowhere in the advertisement does that information appear.

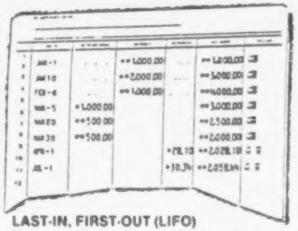
These four banks all pay the same interest rate—yet interest payments range from $44.93 to $75.30



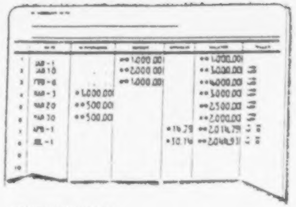
DAY-OF-DEPOSIT to DAY-OF-WITHDRAWAL
Under this arrangement the bank pays you interest for the actual number of days the money remains in the account. This method, which is sometimes called daily interest, instant interest, or day-in day-out is the fairest to consumers. It is used by almost 50 percent of commercial banks and 60 percent of insured S&L's (there are no industry figures for savings banks). It yields the greatest return.
Interest: $75.30



FIRST- IN, FIRST- OUT (FIFO)
With this method, withdrawals are deducted first from the starting balance of the interest period and then, if the balance isn't sufficient, from later deposits. This erodes the base on which your interest is figured and means you automatically lose interest on withdrawals from the start of the interest period rather than from the dates on which the withdrawals were actually made. Another variation of this method is to apply the first withdrawal to the first deposit rather than to the beginning balance; this would earn $53.93. About 16 percent of commercial banks use the FIFO methods according to the ABA.
Interest: $52.44



LAST-IN, FIRST-OUT (LIFO)
Under this plan, withdrawals are deducted from the most recent deposits in the quarter and then from the next most recent ones. This method which does not penalize savers as much as the two FIFO methods is used by about 5 percent of commercial banks.
Interest: $58.44

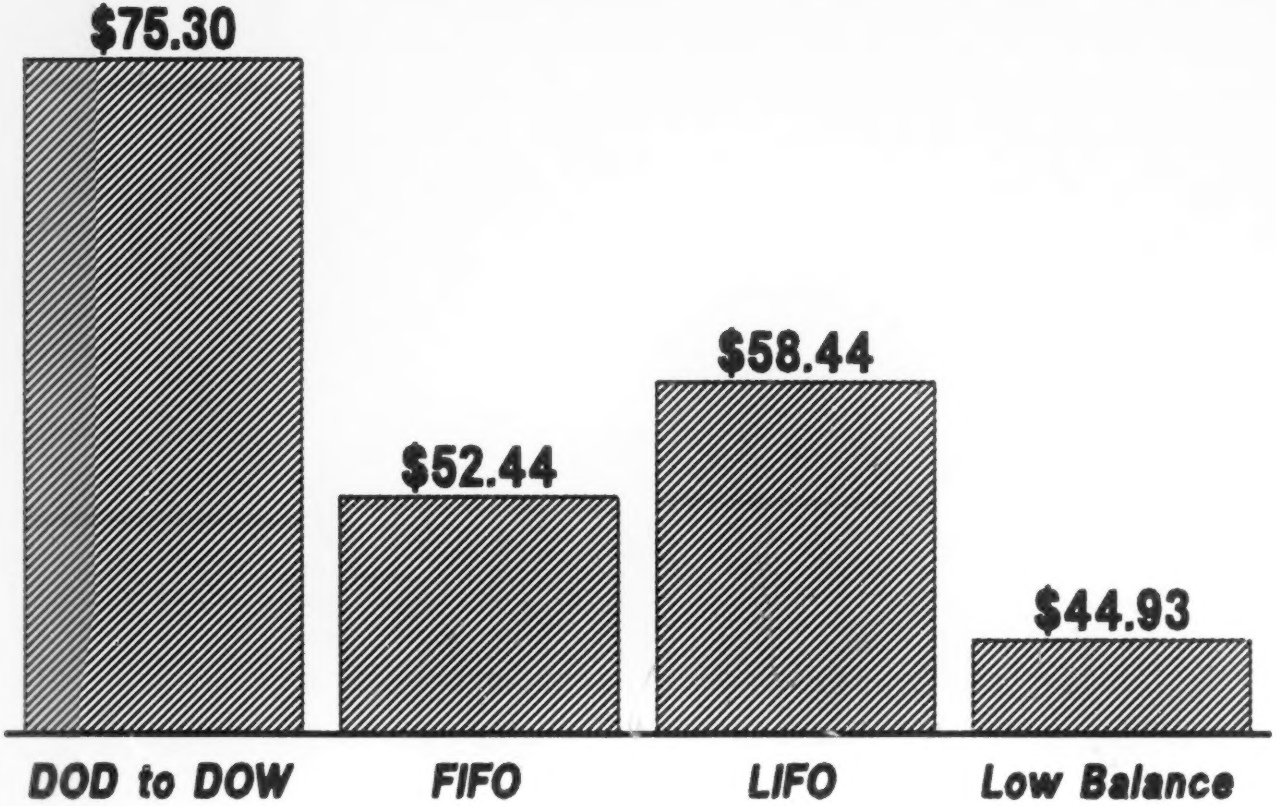


LOW BALANCE
Under this method, interest is paid only on the smallest amount of money that was in the account during the interest period. Despite a balance that reached $4000 during the first quarter, this account earned interest only on $1000—the lowest balance during that period. There are no withdrawals during the second quarter, so the low-balance formula is not important there. This method, which tends to discourage deposits is the most punitive to savers. Yet 30 percent of commercial banks still use it, according to a study last year by the American Bankers Association.
Interest: $44.93

There are many ways of computing interest, as the text of our report indicates. Here are four passbooks showing the identical deposits and withdrawals (made on the same days), with explanations of how the interest has been computed under four common methods. All four assume a six percent interest rate and quarterly crediting and compounding.

Consumer Reports, Feb. 1975

INTEREST VARIES BY CALCULATION METHOD



High Interest. Free Checking.

Money Mgr.

High interest. Free checking. Lots of banks use these words. But how many use them together in the same sentence? Perpetual does. Because with Money Mgr from Perpetual you can have high interest and free checking in a variety of ways.

With an Interest checking account or a Market Rate checking account, you'll be assured of receiving highly competitive rates. And by using Direct Deposit, maintaining a minimum balance, or simply by being a Senior Citizen over 60, your checking account will be absolutely free.

To find out more, visit any Perpetual Banking Center, or call Convenience Banking at 703-838-6110 or 800-422-6540, ext. 6110. Because when it comes to high interest and free checking, we don't just use these words. We stand by them.

6%
Market Rate Checking Account*
6.18

[illegible]

[illegible]

[illegible]

PERPETUAL
What Your Bank is Going To Be.

These are only a couple of examples of how consumers are not getting the bargain that they think they are getting. With the enormous proliferation of fees that have accompanied deregulation a consumer needs to have an IQ of an Einstein to figure out the relative merits of different accounts.

S. 1507 is designed to give consumers a compass by which they can get through the forest of permutations and combinations.

Let me add that when I use the word "bank" I'm referring to all depository institutions as well as to money market mutual funds.

Today's hearing will explore solutions to this account term mania. This issue is extremely important because competition cannot work successfully if consumers cannot fairly and simply compare products. In such markets consumers do not get what they think they are bargaining for. At the same time dishonest banks benefit and honest banks suffer.

Before turning to the other members of the subcommittee, I would like to point out some of the problems presented by the noncomparable information and the failure of disclosure and relevent other terms and conditions that are especially important in the 1980's when there are more and more two worker families and people simply don't have the time needed to identify everything the banks aren't telling them.

I hope that this hearing will help us to determine ways to enable consumers to get the information necessary to easily compare different interests and varying accounts without placing an undue burden on the provisions of such accounts.

I might add that this subcommittee will continue to examine these kinds of problems in the fall as we look to both home equity lines of credit and more generally the ability of consumers to plan their financial affairs.

Now we had hoped to have as our first witness Congressman Lehman, who was going to be here, but is unavoidably detained. He may show up momentarily.

So we'll skip immediately to Mr. Howard Brown. I'm delighted to welcome you, Howard, to the committee. I should tell the committee that this happens to be a good personal friend of mine. We are very fortunate indeed in Connecticut to have Howard as our Commissioner of Banking in the State of Connecticut.

I'm delighted, Howard, that you could come down this afternoon for these hearings. We look forward to your testimony and the questions to be submitted to you.

By the way, I apologize. I didn't see my colleague from Colorado walk in before beginning with you, Howard.

Do you have any opening comments?

OPENING STATEMENT OF SENATOR WIRTH

Senator WIRTH. Thank you very much, Mr. Chairman.

I wanted to, first of all, commend you on having this hearing and for focusing on a number of important consumer issues related to our financial institutions.

I just wanted to note briefly, Mr. Chairman, that we have all approved the FSLIC legislation, and in that legislation, as you know, is the moratorium period. It is now the responsibility of Congress to focus on the restructuring of our financial institutions.

Part of that I think is ultimately going to fall into this important Subcommittee on Consumer Affairs and your jurisdiction looking at the access that individuals have to checking accounts, looking at other problems of very real individual consumer access in poor areas of cities—the kind of issues that you've been involved with for a long period of time.

There is an important responsibility for us there, and I hope that we have on the subcommittee the opportunity to look at some of those possibilities this fall. I think we have a real opportunity on behalf of a lot of people in this country who don't have access any more to the use of financial institutions to do what we can to assure that they do.

Senator DODD. I'm delighted to hear you say that and I appreciate the kind comments and you're absolutely correct.

And for just a second to digress a bit, Howard, and yet really not digress because, as Senator Wirth has pointed out, there is a relationship here. I think one of the problems we saw in the past in dealing with the whole question of financial institutions and what the landscape ought to look like is that we've spent an inordinate amount of time listening to the providers of those services, which is extremely important and obviously you could not draft legislation intelligently without having those kinds of hearings.

But I think we have paid far too little attention to the users of financial institutions and how they would be affected by whatever steps the Congress might take, whether it's with regard to an appeal of Glass-Steagall or opening up certain activities to banks that have otherwise heretofore been foreclosed, we need to look at the impact on the consumer, and the consumer goes from the individual depositor to the corporation in this country that utilizes those services.

I feel confident that the full committee will be conducting hearings that will examine that. To the extent they don't cover the user aspect of that discussion that is ongoing and will continue I presume through the fall into the latter part of this year as we begin to move on a piece of legislation, then certainly this subcommittee will try and pick up that slack so that we focus on how individuals, small businesses, medium and large and others would be impacted as a result of a decision that may be very favorably received by the providers, but could have adverse impact on the users.

So I appreciate your comments.

Senator WIRTH. We are getting requests from a variety of institutions to move into the financial area. They're saying well please let us in, lower these barriers and let's have a "level playing field".

Well, you and I both know that we don't have a level playing field. Institutions are treated in a different way. I think what we want to do, and one of the things that is very promising, is to look at what kind of quid pro quos may be around. We live with that all the time.

If institutions get into the financial services area, what obligations should we ask them to assume? We have done that for a long time. Savings and loans initially had the obligation for looking at home loans, and we had very specific responsibilities to insurance, to commercial banks and to investment banks. Maybe we should be building into this, Mr. Chairman, an obligation to look at consumers as well, just as we have in these other broad areas, and to look at it sort of from the bottom up, as you're suggesting, rather than the top down.

I think we have some very real opportunities here, and I know that under your chairmanship the subcommittee will be able to help us realize those.

I thank you very much.

Senator **Dodd**. Thank you.

Senator **Wirth**. Mr. Brown, I thank you for being here. I'm sorry we're taking away from your time.

Mr. **Brown**. That's quite all right, Senator.

Senator **Dodd**. Senator Chafee. My peripheral vision is getting better all the time. I apologize.

Senator **Chafee**. I have a statement that I'll just put in the record.

Senator **Dodd**. Without objection, it's so ordered and it will be entered along with a statement of Senator Heinz.

STATEMENT OF SENATOR JOHN H. CHAFEE

Senator **Chafee**. Mr. Chairman, I applaud your prompt advancement of this bill, the Truth in Savings Act, for the deliberations of this subcommittee and the full committee. I would ask that you list me as a co-sponsor.

The days of single-rate, fixed-rate accounts have been replaced by a cornucopia of possible accounts with an amazing and unexpected variety of related income and cost aspects. This is increasingly prevalent as financial institutions continue to unbundle their services.

I for one do not underrate the desire and innate ability of the American consumer to choose among these options what is best for him or her; if I felt otherwise, democracy would be less appealing. But the ability to choose is meaningless without the tools of informed choice, and the consumer must have the facts presented in such a fashion as to facilitate not hinder that selection.

From an efficiency point of view, the ideal world would have all accounts using identical terminology, calculation, fee charges, and format; comparability would not then be a problem. But this conflicts somewhat with our notions of competitions and choice. A middle ground must be sought which preserves the right of financial institutions to offer different products, while at the same time presenting the consumer with an understandable choice. Now is the time to create those benchmarks of terminology, calculation and disclosure.

Legislation, or action by the banking regulatory authorities, is necessary because of the use of words like "yield" and "annual interest rate" in depository institution advertising with widely different meanings and values. Calculations of interest earned can vary significantly even if consumers are under the general impression that it is based on a day of deposit, day of withdrawal method. In additon there is the "investable balance" method, which does not even pay interest on those funds which banks must legally hold as reserves. Current advertisements may therefore be incomplete and potentially misleading

Mutual funds, regulated by the SEC, provide a useful counterexample. The calculation of yields in advertised money market funds is standardized. Prospectuses, with significant disclosure, must be provided to consumers before they can invest. Despite these to my knowledge, there has not been a hue and cry about reduced options for consumers.

This bill takes a major step in seeking, within 1 year from enactment, clear and uniform disclosure with regard to interest rates offered and fees assessed on depository accounts. For any advertisement, announcement, or solicitation by a depository institution mentioning an interest rate or yield, on interest bearing accounts, the bill requires specific information to be clearly and conspicuously set forth, including the annual percentage yield, the period it is in effect, the minimum balance and time requirements to earn it, and statements concerning interest penalties for early withdrawal and regular fees and other conditions that could reduce the yield. A schedule of all terms and conditions for each class of depository account is called for, and the breadth of its distribution is set forth. Penalties for violations are established.

This bill's approach represents a worthy start and I encourage you, Mr. Chairman, to move forward expeditiously in this matter.

STATEMENT OF SENATOR JOHN HEINZ

Senator HEINZ. Mr. Chairman, I commend you for calling this hearing on S. 1507, the Truth in Savings Act of 1987. I am proud to have joined you and Senator Dodd in introducing this important consumer legislation on July 21, 1987.

As we all know, the deregulation of interest rates and other changes in the financial services marketplace has created a new, highly competitive arena for consumers' deposits. Today, consumers have many more choices in where and how to invest their money. Unfortunately, trying to select the right financial institution and the right financial instrument can be a difficult, if not impossible, task given the vast array of competing, confusing, and sometimes misleading advertisements.

The purpose of the legislation is quite simple. It would require clear and uniform disclosure in the advertisement of interest rates, yields and terms and conditions which can affect the yield on interest bearing accounts.

Mr. Chairman, this is good legislation for both the consumer and the banking industry. The consumer will have the confusing fog of undecipherable terms and numbers lifted and be able to make reasoned choices regarding investment decisions. The banking industry will see the elimination of the "teaser" advertisements offered by a few of their unsavory brethren and be able to compete fairly for depositors' accounts.

Finally, I would note that the timing of this legislation could not be better in that it dovetails with another piece of consumer legislation to prohibit depository institutions from placing lengthy holds on depositors' checks. The check hold legislation is part of the legislation to recapitalize the FSLIC fund. The conference report has been approved by the House and Senate and awaits only the signature of the President for enactment into law.

Mr. Chairman, I hope that the truth-in-savings measure will be a priority item for this committee. It is for me.

I join you in welcoming our witnesses today including, Congressman Lehman, the author of the House version of the bill, and I look forward to hearing their testimony.

[Copy of proposed bill S. 1507 follows:]

II

100TH CONGRESS
1ST SESSION

S. 1507

To provide for the uniform disclosure of the rates of interest which are payable on savings accounts, and for other purposes.

IN THE SENATE OF THE UNITED STATES

JULY 21 (legislative day, JUNE 23), 1987

Mr. PROXMIRE (for himself, Mr. DODD, and Mr. HEINZ) introduced the following bill; which was read twice and referred to the Committee on Banking, Housing, and Urban Affairs

---

A BILL

To provide for the uniform disclosure of the rates of interest which are payable on savings accounts, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. SHORT TITLE.

This Act may be cited as the "Truth in Savings Act".

SEC. 2. FINDINGS AND PURPOSE.

(a) FINDINGS.—The Congress hereby finds that economic stability would be enhanced, competition between depository institutions would be improved, and the ability of the consumer to make informed decisions regarding deposit accounts would be strengthened if there was uniformity in the disclosure of terms and conditions on which interest is paid and fees are assessed in connection with such accounts.

(b) PURPOSE.—It is the purpose of this Act to require the clear and uniform disclosure of—

(1) the rates of interest which are payable on deposit accounts by depository institutions; and

(2) the fees that are assessable against deposit accounts,

so that consumers can make a meaningful comparison between the competing claims of depository institutions with regard to deposit accounts.

SEC. 3. DISCLOSURE OF INTEREST RATES AND TERMS OF ACCOUNTS.

(a) IN GENERAL.—Except as provided in subsection (b), each advertisement, announcement, or solicitation initiated by any depository institution relating to any demand or interest-bearing account which includes any reference to a specific rate of interest payable on amounts deposited in such account, or to a specific yield or rate of earnings on amounts so deposited, shall state the following information, to the extent applicable, in a clear and conspicuous manner:

(1) The annual percentage yield (which shall be noted in greater prominence than any other stated rate).

(2) The period during which such annual percentage yield is in effect.

(3) All minimum account balance and time requirements which must be met in order to earn the advertised yield (and, in the case of accounts for which more than 1 yield is stated, each annual percentage yield and the account minimum balance requirement associated with each such yield shall be in close proximity and have equal prominence).

(4) The minimum amount of the initial deposit which is required to open the account in order to obtain the yield advertised, if such minimum amount is greater than the minimum balance necessary to earn the advertised yield.

(5) The annual rates of simple interest.

(6) A statement that regular fees or other conditions could reduce the yield.

(7) A statement that an interest penalty is required for early withdrawal.

(8) In the case of a certificate of deposit or other account for which the stated date of maturity is less than 1 year, a statement of the effective percentage yield on the date of maturity.

(b) BROADCAST AND ELECTRONIC MEDIA AND OUTDOOR ADVERTISING EXCEPTION.—The Board may, by regulation, exempt advertisements, announcements, or solicitations made by any broadcast or electronic medium or outdoor advertising display not on the premises of the depository institution from any disclosure requirements described in paragraph (4), (5), or (6) of subsection (a) if the Board finds that any such disclosure would be unnecessarily burdensome.

(c) MISLEADING DESCRIPTIONS OF FREE OR NO-COST ACCOUNTS PROHIBITED.—No advertisement, announcement, or solicitation made by any depository institution may refer to or describe an account as a free or no-cost account if—

(1) in order to avoid fees or service charges for any period—

(A) a minimum balance must be maintained in the account during such period; or

(B) the number of transactions during such period may not exceed a maximum number; or

(2) any regular service or transaction fee is imposed.

(d) MISLEADING OR INACCURATE ADVERTISEMENTS, ETC., PROHIBITED.—No depository institution shall make any advertisement, announcement, or solicitation relating to a deposit account that is inaccurate or misleading or that misrepresents its deposit contracts.

SEC. 4. ACCOUNT SCHEDULE.

(a) IN GENERAL.—Each depository institution shall maintain a schedule of fees, charges, interest rates, and terms and conditions applicable to each class of accounts offered by the depository institution, in accordance with the requirements of this section and regulations which the Board shall prescribe. The Board shall specify, in regulations, which fees, charges, penalties, terms, conditions, and account restrictions must be included in a schedule required under this subsection. A depository institution need not include in such schedule any information not specified in such regulation.

(b) INFORMATION ON FEES AND CHARGES.—The schedule required under subsection (a) with respect to any account shall contain the following information:

(1) A description of all fees, periodic service charges, and penalties which may be charged or assessed against the account (or against the account holder in connection with such account), the amount of any such fees, charge, or penalty (or the method by which such amount will be calculated), and the conditions under which any such amount will be assessed.

(2) All minimum balance requirements that affect fees, charges, and penalties, including a clear description of how each such minimum balance is calculated.

(3) Any minimum amount required with respect to the initial deposit in order to open the account

(c) INFORMATION ON INTEREST RATES.—The schedule required under subsection (a) with respect to any account shall include the following information:

(1) Any annual percentage yield.

(2) The period during which any such annual percentage yield will be in effect.

(3) Any annual rate of simple interest.

(4) The frequency with which interest will be compounded and credited.

(5) A clear description of the method used to determine the balance on which interest is paid.

(6) In the case of a certificate of deposit or other account for which the stated date of maturity is less than 1 year, a statement of the effective percentage yield on the date of maturity.

(7) The information described in paragraphs (1) through (4) with respect to any period after the end of the period referred to in paragraph (2) (or the method for computing any information described in any such paragraph), if applicable.

(8) Any minimum balance which must be maintained to earn the rates and obtain the yields disclosed pursuant to this subsection and a clear description of how any such minimum balance is calculated.

(9) A clear description of any minimum time requirement which must be met in order to obtain the yields disclosed pursuant to this subsection and any information described in paragraph (1), (2), (3), or (4) that will apply if any time requirement is not met.

(10) A statement, if applicable, that any interest which has accrued but has not been credited to an account at the time of a withdrawal from the account will not be paid by the depository institution or credited to the account by reason of such withdrawal.

(11) Any provision or requirement relating to nonpayment of interest, including any charge or penalty for early withdrawal, and the conditions under which any such charge or penalty may be assessed.

(d) OTHER INFORMATION.—The schedule required under subsection (a) shall include such other disclosures as the Board may determine to be necessary to allow consumers to understand and compare accounts, including frequency of interest rate adjustments, account restrictions, and renewal policies for time accounts.

(e) STYLE AND FORMAT.—Schedules required under subsection (a) shall be written in clear and plain language and be presented in a format designed to allow consumers to readily understand the terms of the accounts offered.

SEC. 5. DISCLOSURE REQUIREMENTS FOR CERTAIN ACCOUNTS.

The Board shall require, in regulations which the Board shall prescribe, such modification in the disclosure requirements under this Act relating to annual percentage yield as may be necessary to carry out the purposes of this Act in the case of—

(1) accounts with respect to which determination of annual percentage yield is based on an annual rate of interest that is guaranteed for a period of less than 1 year;

(2) variable rate accounts;

(3) accounts which, pursuant to law, do not guarantee payment of a stated rate; and

(4) multiple rate accounts.

SEC. 6. DISTRIBUTION OF SCHEDULES.

(a) IN GENERAL.—A schedule required under section 4 for an appropriate account shall be—

(1) included in any regularly scheduled mailing to holders of that account which occurs not more than 90 days after the effective date of the initial regulations prescribed by the Board under this Act, unless the depository institution has provided, before such effective date, a disclosure which meets the requirements of section 4;

(2) made available to any person upon request; and

(3) provided to any potential customer before an account is opened or a service is rendered.

(b) DISTRIBUTION IN CASE OF CERTAIN INITIAL DEPOSITS.—If—

(1) a depositor is not physically present at an office of a depository institution at the time an initial deposit is accepted with respect to an account established by or for such person; and

(2) the schedule required under section (4)(a) has not been furnished previously to such depositor,

the depositor institution shall mail the schedule to the depositor at the address shown on the records of the depository institution for such account no later than 10 days after the date of the initial deposit.

(c) DISTRIBUTION OF NOTICE OF CERTAIN CHANGES.—If—

(1) any change is made in any term or condition which is required to be disclosed in the schedule required under section 4(a) with respect to any account; and

(2) the change may reduce the yield or adversely affect any holder of the account, all account holders who may be affected by such change shall be notified and provided with a description of the change by mail at least 30 days before the change takes effect.

(d) DISTRIBUTION IN CASE OF ACCOUNTS ESTABLISHED BY MORE THAN 1 INDIVIDUAL OR BY A GROUP.—If an account is established by more than 1 individual or for a person other than an individual, any distribution described in this section with respect to such account meets the requirements of this section if the distribution is made to 1 of the individual who established the account or 1 individual representative of the person on whose behalf such account was established.

SEC. 7. PAYMENT OF INTEREST.

(a) CALCULATED ON FULL AMOUNT OF PRINCIPAL.—The amount of interest accruing on an interest-bearing account at any depository institution shall be calculated by such institution on the full amount of principal in the account for the stated calculation period at the rate or rates of interest disclosed pursuant to this Act.

(b) NO PARTICULAR METHOD OF COMPOUNDING INTEREST REQUIRED.—Subsection (a) shall not be construed as prohibiting or requiring the use of any particular method of compounding or crediting of interest.

SEC. 8. REGULATIONS.

(a) IN GENERAL.—Not later than 1 year after the date of the enactment of this Act, the Board, after consultation with each agency referred to in section 9(a) and public notice and opportunity for comment, shall prescribe regulations to carry out the purpose and provisions of this Act. The regulations so prescribed may contain such classifications, differentiations, or other provisions, and may provide for such adjustments and exceptions for any class of accounts as, in the judgment of the Board, are necessary or proper to carry out the purposes of this Act, to prevent circumvention or evasion of the requirements of this Act, or to facilitate compliance with the requirements of this Act.

(b) MODEL FORMS AND CLAUSES.—

(1) IN GENERAL.—The Board shall publish model forms and clauses for common disclosures to facilitate compliance with this Act. In devising such forms, the Board shall consider the use by depository institutions of data processing or similar automated machines.

(2) USE OF FORMS AND CLAUSES DEEMED IN COMPLIANCE.—Nothing in this Act may be construed to require a depository institution to use any such model form or clause prescribed by the Board under this subsection. A depository institution shall be deemed to be in compliance with the disclosure provisions of this Act if the depository institution—

(A) uses any appropriate model form or clause as published by the Board; or

(B) uses any such model form or clause and changes it by—

(i) deleting any information which is not required by this Act; or

(ii) rearranging the format,

if in making such deletion or rearranging the format, the depository institution does not affect the substance, clarity, or meaningful sequence of the disclosure.

(3) PUBLIC NOTICE AND OPPORTUNITY FOR COMMENT.—Model disclosure forms and clauses shall be adopted by the Board after duly given notice in the Federal Register and an opportunity for public comment in accordance with section 553 of title 5, United States Code.

SEC. 9. ADMINISTRATIVE ENFORCEMENT.

(a) IN GENERAL.—Compliance with the requirements imposed under this Act shall be enforced under—

(1) section 8 of the Federal Deposit Insurance Act, in the case of—

(A) national banks, by the Comptroller of the Currency;

(B) member banks of the Federal Reserve System (other than national banks), by the Board; and

(C) depository institutions described in clause (i), (ii), or (iii) of section 19(b)(1)(A) of the Federal Reserve Act (other than member banks of the Federal Reserve System) by the Board of Directors of the Federal Deposit Insurance Corporation;

(2) section 5(d) of the Home Owners' Loan Act of 1933, section 407 of the National Housing Act, and sections 6(i) and 17 of the Federal Home Loan Bank Act, by the Federal Home Loan Bank Board (acting directly or through the Federal Savings and Loan Insurance Corporation) in the case of depository institutions described in clause (v) or (vi) of section 19(b)(1)(A) of the Federal Reserve Act; and

(3) the Federal Credit Union Act, by the National Credit Union Administration Board in the case of depository institutions described in clause (iv) of section 19(b)(1)(A) of the Federal Reserve Act.

(b) Additional Enforcement Powers.—

(1) Violation of this act treated as violation of other acts.—For purposes of the exercise by any agency referred to in subsection (a) of such agency's powers under any Act referred to in such subsection, a violation of a requirement imposed under this

Act shall be deemed to be a violation of a requirement imposed under that Act.

(2) Enforcement authority under other acts.—In addition to the powers of any agency referred to in subsection (a) under any provision of law specifically referred to in such subsection, each such agency may exercise, for purposes of enforcing compliance with any requirement imposed under this Act, any other authority conferred on such agency by law.

(c) Regulations by Agencies Other Than the Board.—The authority of the Board to issue regulations under this Act does not impair the authority of any other agency referred to in subsection (a) to make rules regarding its own procedures in enforcing compliance with the requirements imposed under this Act.

SEC. 10. CIVIL LIABILITY.

(a) Civil Liability.—Except as otherwise provided in this section, any depository institution which fails to comply with any requirement imposed under this Act or any regulation prescribed under this Act with respect to any person is liable to such person in an amount equal to the sum of—

(1) any actual damage sustained by such person as a result of the failure;

(2)(A) in the case of an individual action, such additional amount as the court may allow, except that the liability under this subparagraph shall not be less than $100 nor greater than $1,000; or

(B) in the case of a class action, such amount as the court may allow, except that—

(i) as to each member of the class, no minimum recovery shall be applicable; and

(ii) the total recovery under this subparagraph in any class action or series of class actions arising out of the same failure to comply by the same depository institution shall not be more than the lesser of $500,000 or 1 percent of the net worth of the depository institution involved; and

(3) in the case of any successful action to enforce any liability under paragraph (1) or (2), the costs of the action, together with a reasonable attorney's fee as determined by the court.

(b) Class Action Awards.—In determining the amount of any award in any class action, the court shall consider, among other relevant factors—

(1) the amount of any actual damages awarded;

(2) the frequency and persistence of failures of compliance;

(3) the resources of the depository institution;

(4) the number of persons adversely affected; and

(5) the extent to which the failure of compliance was intentional.

(c) Bona Fide Errors.—

(1) General rule.—A depository institution may not be held liable in any action brought under this section for a violation of this Act if the depository institution demonstrates by a preponderance of the evidence that the violation was not intentional and resulted from a bona fide error, notwithstanding the maintenance of procedures reasonably adapted to avoid any such error.

(2) Examples.—Examples of a bona fide error include clerical, calculation, computer malfunction and programming, and printing errors, except that an error of legal judgment with respect to a depository institution's obligation under this Act is not a bona fide error.

(d) Jurisdiction.—Any action under this section may be brought in any United States district court, or in any other court of competent jurisdiction, within one year after the date of the occurrence of the violation involved.

(e) Reliance on Board Rulings.—No provision of this section imposing any liability shall apply to any act done or omitted in good faith in conformity with any rule, regulation, or interpretation thereof by the Board, notwithstanding the fact that after such act or omission has occurred, such rule, regulation, or interpretation is amended, rescinded, or determined by judicial or other authority to be invalid for any reason.

(f) NOTIFICATION OF AND ADJUSTMENT FOR ERRORS.—A depository institution shall not be liable under this section or section 9 for any failure to comply with any requirement imposed under this Act with respect to any account if—

(1) before—

(A) the end of the 60-day period beginning on the date on which the depository institution discovered the failure to comply;

(B) any action is instituted against the depository institution by the account holder under this section with respect to such failure to comply; and

(C) any written notice of such failure to comply is received by the depository institution from the account holder,

the depository institution notifies the account holder of the failure of such institution to comply with such requirement; and

(2) the depository institution makes such adjustments as may be necessary with respect to such account to ensure that—

(A) the account holder will not be liable for any amount in excess of the amount actually disclosed with respect to any fee or charge;

(B) the account holder will not be liable for any fee or charge imposed under any condition not actually disclosed; and

(C) interest on amounts in such account will accrue at the annual percentage yield, and under the conditions, actually disclosed (and credit will be provided for interest already accrued at a different annual percentage yield and under different conditions than the yield or conditions disclosed).

(g) MULTIPLE INTERESTS IN 1 ACCOUNT.—If more than 1 person holds an interest in any account—

(1) the minimum and maximum amounts of liability under subsection (a)(2)(A) for any failure to comply with the requirements of this Act shall apply with respect to such account; and

(2) the court shall determine the manner in which the amount of any such liability with respect to such account shall be distributed among such persons.

(h) CONTINUING FAILURE TO DISCLOSE.—

(1) CERTAIN CONTINUING FAILURES TREATED AS 1 VIOLATION.—Except as provided in paragraph (2), the continuing failure of any depository institute to

disclose any particular term required to be disclosed under this Act with respect to a particular account shall be treated as a single violation for purposes of determining the amount of any liability of such institution under subsection (a) for such failure to disclose.

(2) SUBSEQUENT FAILURE TO DISCLOSE.—The continuing failure of any depository institution to disclose any particular term required to be disclosed under this Act with respect to a particular account after judgment has been rendered in favor of the account holder in connection with a prior failure to disclose such term with respect to such account shall be treated as a subsequent violation for purposes of determining liability under subsection (a).

(3) COORDINATION WITH SECTION 9.—This subsection shall not limit or otherwise affect the enforcement power under section 9 of any agency referred to in subsection (a) of such section.

SEC. 11. CREDIT UNIONS.

(a) IN GENERAL.—No regulation prescribed by the Board under this Act shall apply directly with respect to any depository institution described in clause (iv) of section 19(b)(1)(A) of the Federal Reserve Act.

(b) REGULATIONS PRESCRIBED BY THE NCUA.—Within 90 days of the effective date of any regulation prescribed by the Board under this Act, the National Credit Union Administration Board shall prescribe a regulation substantially similar to the regulation prescribed by the Board taking into account the unique nature of credit unions and the limitations under which they may pay dividends on member accounts.

SEC. 12. EFFECT ON STATE LAW.

This Act does not annul, alter, or affect the laws of any State relating to the disclosure of information in connection with terms of deposit accounts, except to the extent that those laws are inconsistent with the provisions of this Act, and then only to the extent of the inconsistency.

SEC. 13. DEFINITIONS

For the purposes of this Act—

(1) DEPOSITORY INSTITUTION.—The term "depository institution" has the meaning given such term in clauses (i) through (vi) of section 19(b)(1)(A) of the Federal Reserve Act.

(2) BOARD.—The term "Board" means the Board of Governors of the Federal Reserve System.

(3) ACCOUNT.—The term "account" means any account offered to 1 or more individuals or an unincorporated nonbusiness association of individuals by a depository institution into which a customer deposits funds, including demand accounts, time accounts, nego-

Senator **Dodd**. Howard, again, proceed.

STATEMENT OF HOWARD B. BROWN, COMMISSIONER OF BANKING, THE STATE OF CONNECTICUT

Mr. **Brown**. Thank you.

Mr. Chairman and distinguished members of the Consumer Affairs Subcommittee, my name is Howard B. Brown. I am Banking Commissioner of the State of Connecticut.

It is with great pleasure that I address you today, and I am particularly pleased to join with my Senator from the Constitution State, Christopher J. Dodd, in support of S. 1507, the Truth in Savings Act.

As Banking Commissioner my responsibility is to protect the citizens of Connecticut by ensuring the safety and soundness of our financial institutions, depository as well as others.

To uphold this charge means not only protecting the funds which consumers place in the hands of our banking institutions, but of equal importance, protection from misleading information which might jeopardize those funds or the confidence that consumers should have when placing their money in savings accounts.

Fortunately, in Connecticut we are well equipped with laws that govern the manner by which banking institutions solicit the public and the disclosures that are necessary for savings accounts.

Chapter 637(a) of the Connecticut General Statutes, which was enacted in 1979 and amended in 1981, a copy of which has been submitted for the record, provides that banking institutions shall provide individual depositors with a deposit contract and a schedule of charges prior to opening a savings account.

PROVIDING SCHEDULE OF INTEREST RATES

Financial institutions, other than credit unions, are also required to provide the depositor with a schedule of interests prior to the opening of each new savings account. Whenever the simple interest on a savings account is reduced, our institutions must post a notice of the change or an updated schedule of interest in their offices within 15 days after the change.

The institutions must also deliver a notice of the change with the next subsequent periodic statement, if any, after the change.

In Connecticut our laws work. It was therefore a great comfort for me to review the provisions which are set forth in S. 1507 to compare them with the provisions of the Connecticut law. I am delighted to report that six of the provisions of your Truth in Savings legislation are part of the Connecticut's Deposit Account Contract Act.

Two of the provisions which you have included in S. 1507 are not found in our law. One has to do with the annual percentage yield being placed in greater prominence than any other stated rate. This is not included in our law because we do not address the issue of advertising as pertains to savings account contracts.

The FDIC, on the other hand, does address advertising requirements in section 329.3 of its rules and regulations. Should the Connecticut Department of Banking become aware of any violations of

FDIC regulations, we routinely refer such cases to the FDIC authorities.

The other provision currently not found in our Connecticut statute pertains to your recommendation that a statement of the effective percentage yield on the date of maturity be provided to consumers in the case of a certificate of deposit or other account for which the stated date of maturity is less than 1 year.

The explanation for not having such a provision in Connecticut's Deposit Account Contract Act is understandable. In 1979 and again in 1981 the popularity and availability of certificates of deposit were far from what they are today. Minimum amount restrictions were so great that the average consumer was not able to avail himself of those types of accounts.

In today's business environment where each and every one of us is seeking ways to obtain the higher return for our savings, the CD account is commonplace. This may very well be the time to wisely explain through the proposed legislation the differences which may exist in effective annual yield versus effective percentage yield at the date of maturity.

SAVERS HAVE MANY CHOICES OF SERVICES

You're correct, Senator Dodd, in your assertion that today's saver has more choices than ever before. There are literally scores of services being offered to consumers by depository institutions.

For example, Senator, you expressed interest in my views as to whether this legislation should include mutual funds. I see no reason why the disclosure provisions of this legislation should not apply uniformly to mutual funds as well.

After all, the basic issue is the protection of the consumer. Uniform disclosure requirements should apply across the board, in my humble opinion, to all savings instruments available to the consumer. This is why it is imperative that Congress and the banking regulators identify and implement the methods that can best disclose the benefits and disadvantages of these various services to consumers in such a way that will not compound confusion as well as compound the funds.

Passage of S. 1507 would lawfully spell out the methods that are to be used for savings accounts. Let's do what we can to spell it out, but let's avoid creating situations whereby the language of the law becomes cumbersome and hard for the average bank customer to comprehend.

We all know there are many bank customers who shop around for the best way to invest their money in savings accounts. These consumers are elitists. They know what to look for and they understand the terms which are being marketed and which they are being solicited of.

The majority of bank customers, however, are not as sophisticated and do not have the time to shop around, but they, too, want to get the most for their money. That is why Federal and State regulators must ensure that our country's financial institutions rely on simple but honest terms in the advertising and promotion of savings accounts.

Thank you, Senator, for hearing my testimony.

[The complete prepared statement of Howard Brown follows:]

tiable order of withdrawal accounts, and share draft accounts.

(4) Interest.—The term "interest" includes dividends paid with respect to share draft accounts which are accounts within the meaning of paragraph (3).

(5) Multiple rate account.—The term "multiple rate accounts" means any account that has 2 or more annual rates of simple interest which take effect in succeeding periods and which are known at the time of disclosure.

(6) Annual percentage yield.—The term "annual percentage yield" shall be equal to the total amount of interest that would be received on a $100 deposit under the terms described in paragraphs (3) and (4) of section 4(c) over a year, expressed as a percentage calculated by a method which shall be prescribed by the Board in regulations.

○

TESTIMONY OF

HOWARD B. BROWN

Mr. Chairman, and distinguished members of the Consumer Affairs Subcommittee, my name is Howard B. Brown. I am Banking Commissioner of the State of Connecticut.

It is with great pleasure that I address you today and I am particularly pleased to join with my Senator from the Constitution State, Christopher J. Dodd, in support of S. 1507, the Truth in Savings Act.

As Banking Commissioner, my responsibility is to protect the citizens of Connecticut by insuring the safety and soundness of our financial institutions. To uphold this charge means not only protecting the funds which consumers place in the hands of our banking institutions, but, of equal importance, protection from misleading information which might jeopardize these funds or the confidence that customers should have when placing their money in savings accounts.

Fortunately, in Connecticut we are well equipped with laws that govern the manner by which banking institutions solicit the public and the disclosures that are necessary for savings accounts.

Chapter 637a of the Connecticut General Statutes, which was enacted in 1979 and amended in 1981, a copy of which is submitted for the record, provides that banking institutions shall provide individual depositors with a deposit contract and a schedule of charges prior to opening a new savings account. Financial institutions, other than credit unions, are also required to provide the depositor with a schedule of interest prior to the opening of each new savings account.

Whenever the simple interest rate on a savings account is reduced, our institutions must post a notice of the reduction, or an updated schedule of interest, in their offices within 15 days after the change. The institutions must also deliver a notice of the reduction with the next subsequent periodic statement, if any, after the reduction.

In Connecticut, our law works! It was therefore a great comfort for me to review the provisions you set forth in S. 1507 to compare them with the provisions of the Connecticut law. I am delighted to report that six of the provisions of your "Truth in Savings" legislation are part of Connecticut's Deposit Account Contract Act.

Two of the provisions which you've included in S. 1507 are not found in our law. One has to do with the annual percentage yield being placed in greater prominence than any other stated rate. This is not included in our law because we do not address the issue of advertising as it pertains to savings account contracts. The FDIC, on the other hand, does address advertising requirements in Section 329.3 of its Rules and Regulations. Should the Connecticut Department of Banking become aware of any violations of FDIC regulations, we routinely refer such cases to FDIC authorities.

The other provision currently not found in our Connecticut statute pertains to your recommendation that a statement of the effective percentage yield on the date of maturity be provided to consumers in the case of a certificate of deposit or other account for which the stated date of maturity is less than one year.

The explanation for not having such a provision in Connecticut's rather comprehensive Deposit Account Contract ACT is understandable. In 1979, and again in 1981, the popularity and availability of certificates of deposit were far from what they are today. Minimum amount restrictions were so great that the average consumer was not able to avail himself or herself of those types of accounts.

In today's business environment where each and every one of us is seeking ways to obtain a higher return for our savings, the CD account is commonplace. This may very well be the time to wisely explain the differences in effective annual yield versus an effective percentage yield at the date of maturity.

Senator Dodd, you are correct in your assertion that "today's saver has more choices than ever before." There are literally scores of services being offered to consumers by depository institutions. For example, Senator, you expressed interest in my views as to whether this legislation should include mutual funds. I see no reason why the disclosure provisions of this legislation should not apply to mutual funds. Afterall, the basic issue is the protection of the consumer. Disclosure requirements should apply across the board to all savings instruments available to the consumer.

This is why it is imperative that Congress, and the banking regulators, identify and implement the methods that can best explain the benefits and disadvantages of these various services to consumers in such a way that will not compound confusion along with their money.

Passage of S. 1507 would lawfully spell out the methods that are to be used for savings accounts. Let's do what we can to spell it out but let's avoid creating situations whereby the language of the law becomes cumbersome and hard for the average bank customer to comprehend. We all know there are many bank customers who shop around for the best way to invest their money in savings accounts. These consumers are elitists. They know what to look for no matter what terms are used in marketing a savings account.

The majority of bank customers, however, are not as sophisticated and do not have the time to shop around. But they, too, want to get the most from their money. That is why federal and state regulators must insure that our country's financial institutions rely on simple, but honest, terms in the advertising and promotion of savings accounts. That, distinguished members of The Committee, is the bottom line. Regulation, at the convenience, rather than at the confusion, of the consumer.

Thank you.

CHAPTER 637a

DEPOSIT ACCOUNT CONTRACT ACT

Sec. 36-27a. Short title. This chapter shall be known and may be cited as the "Deposit Account Contract Act."

(P.A. 79-433, S. 1, 11.)

History: P.A. 79-433 effective July 1, 1980

Sec. 36-27b. Definitions. As used in this chapter:

(a) "Commissioner" means the banking commissioner.

(b) "Deliver" means deliver in person or place in the United States mail with first class postage properly affixed.

(c) "Deposit" means any deposit, as defined in subsection (c) of section 36-2, and the payment on a share or time share at a credit union or federal credit union.

(d) "Deposit account" means any account at a financial institution (1) which is in the name of one or more natural persons, (2) in which, with regard to a trust account, the entire beneficial interest is held by one or more natural persons, and (3) into which

deposits may be made. "Deposit account" does not include a general or limited partnership account or a sole proprietorship business account.

(e) "Deposit contract" means the contract between a financial institution and a depositor that sets forth the terms, conditions, duties and obligations relating to a deposit account.

(f) Except as provided in subsection (d) of section 36-27i, "depositor" means any natural person who is legally entitled to make withdrawals or sell shares from a deposit account at a financial institution regardless of whether a penalty may be imposed for such withdrawal or sale.

(g) "Earning period" means the period during which interest accrues and at the end of which accrued interest is credited to a savings or time account.

(h) "Financial institution" means any state bank and trust company, national banking association, savings bank, savings and loan association, federal savings and loan association, credit union, federal credit union or federal savings bank.

(i) "Office" of a financial institution does not include an automated teller machine, satellite device or point of sale terminal.

(j) "Post" means to post or otherwise provide notice in a location so that such notice is easily visible to depositors. With regard to an office at which a financial institution lacks access to space for posting notices, such as an office within a retail establishment, "post" means to make available to any depositor upon request.

(k) "Savings deposit" means a savings deposit, as defined in subsection (f) of section 36-2, and the payment on shares at a credit union or federal credit union, and a "savings account" is a deposit account which contains savings deposits.

(l) (1) "Schedule of deposit account charges" means a chart reciting each charge which may be imposed on a depositor for utilizing the services of a financial institution with regard to a deposit account, including, without limitation, charges for: (A) Stop payment orders; (B) items drawn on a deposit account which are dishonored; (C) providing the depositor with a copy of any record relating to a deposit account; (D) the use of checks, negotiable orders of withdrawal, share drafts, or other items, devices or methods that may be used to withdraw moneys from a deposit account; and (E) maintaining a deposit account, such as service charges. (2) If a charge will be imposed only if certain conditions are met or not met, such conditions shall also be recited in such schedule. Such conditions shall include, but not be limited to, failure to maintain a minimum balance in a deposit account. (3) A schedule of deposit account charges is "current" as to any depositor if any changes from the schedule delivered to such depositor in accordance with section 36-27d were made in accordance with section 36-27f.

(m) (1) "Schedule of interest" means a chart reciting for any savings or time account: (A) The annual rate of simple interest that will be paid on such account; (B) the effective annual percentage yield that will be paid on such account; (C) the frequency with which interest will be compounded and the frequency with which interest will be credited to such account; (D) the minimum amount which must be deposited in such account to open such account; (E) the minimum balance that must be maintained in such account in order for interest to be credited to such account; and (F) any condition relating to maintenance of a minimum balance for any part of the earning period which may cause interest not to be credited to such account at the end of the earning period.

(2) For any time account which has an interest rate that may vary from term to term, the annual rate of simple interest and effective annual percentage yield that will be paid on such account may be recited in the schedule of interest as follows: "This rate varies. To determine the current rate, call ____ (telephone number) on any business day."

(3) A schedule of interest is "current" as to any depositor if any changes from the schedule delivered to such depositor in accordance with section 36-27d were made in accordance with section 36-27g.

(n) "Time deposit" means a time deposit as defined in subsection (e) of section 36-2, and a credit union member's payment on shares which such member agrees in writing not to withdraw within the time period stated therein as described in subdivision (b) of subsection (8) of section 36-200. A "time account" is a deposit account which contains time deposits.

(P.A. 79-433, S. 2, 11; P.A. 81-261, S. 1.)

History: P.A. 79-433 effective July 1, 1980; P.A. 81-261 inserted new Subsecs. (b), (i) and (j) to define "deliver", "office" and "post" respectively and relettered the remaining Subsecs. accordingly, amended Subsec. (d) to redefine "deposit account", amended Subsec. (m) to provide that the schedule of interest recite the minimum amount which must be deposited to open an account and provide a format to recite the rate of simple interest and effective annual percentage yield when the interest rate varies, and rephrased and clarified certain of the other definitions.

Sec. 36-27c. Prohibited acts of financial institutions. (a) Except as otherwise provided in this chapter, no financial institution shall enforce or attempt to enforce any material term, condition, duty or obligation other than those required by law, federal or state governmental regulation, rule or order, court order or clearinghouse rule on any depositor with regard to a deposit account that is opened on or after July 1, 1980, unless such term, condition, duty or obligation is included in the deposit contract governing such account. The provisions of title 42a are "required by law" for the purposes of this subsection to the extent that such provisions are not varied by agreement.

(b) No financial institution shall impose or attempt to impose any charge that is not recited in, or is in an amount greater than recited in, the current schedule of deposit account charges.

(c) No financial institution, other than a credit union or federal credit union, shall pay or attempt to pay interest at a lower effective annual percentage yield than that recited in the current schedule of interest.

(P.A. 79-433, S. 3, 11; P.A. 81-261, S. 2.)

History: P.A. 79-433 effective July 1, 1980; P.A. 81-261 amended Subsec. (a) by adding "except as otherwise provided in this chapter", replacing "impose" with "enforce" and providing that the provisions of title 42a are required by law to the extent that such provisions are not varied by agreement, and amended Subsecs. (b) and (c) by replacing "listed" with "recited".

Sec. 36-27d. Copy of deposit account contract and schedule of charges and interest to be furnished to depositors. Exceptions. (a) Except as provided in subsection (b) of this section, prior to opening a new deposit account for any depositor or prospective depositor: (1) Each financial institution shall deliver to such depositor or prospective depositor a copy of the deposit contract, a schedule of deposit account

charges and, if such account is a time account, a schedule of interest, that govern such account; and (2) each financial institution, other than a credit union or federal credit union, shall deliver to each depositor or prospective depositor a schedule of interest that governs such account if such account is a savings account.

(b) If all or any part of a maturing or otherwise expiring time deposit is deposited by renewal, roll-over or otherwise in a new deposit account within thirty days after expiration, the provisions of subsection (a) of this section shall not apply to such new account, except that if the effective annual percentage yield on such new account is lower than the effective annual percentage yield on the expiring account, prior to opening such new account the financial institution shall deliver to the depositor a copy of the schedule of interest governing the new account. The provisions of this subsection shall be inapplicable if the expiring time account was opened prior to July 1, 1980.

(P.A. 79-433, S. 4, 11; P.A. 81-261, S. 3.)

History: P.A. 79-433 effective July 1, 1980; P.A. 81-261 rephrased the section and added Subsec. (b) to provide that the provisions of Subsec. (a) do not apply to an expiring time deposit which is renewed, rolled-over or otherwise deposited in a new account, except if the effective annual percentage yield on the new account is less than that on the expiring account the financial institution shall deliver a schedule of interest prior to the opening of the new account.

Sec. 36-27e. Schedule of interest and charges to be posted. Each financial institution, other than a credit union or federal credit union, shall post a current schedule of interest and each financial institution shall post a current schedule of deposit account charges in each office at which deposits are accepted.

(P.A. 79-433, S. 5, 11; P.A. 81-261, S. 4.)

History: P.A. 79-433 effective July 1, 1980; P.A. 81-261 deleted the requirement that the schedules be posted in a location easily visible to depositors.

Sec. 36-27f. Changes in deposit account charges. Notice. A financial institution may delete or decrease any existing deposit account charges without notice. No financial institution shall impose any new deposit account charge or increase any existing deposit account charge unless the financial institution: (1) At least thirty days prior to such imposition or increase, posts a notice reciting such new or increased charge adjacent to, or incorporates such notice in, the current schedule of deposit account charges posted in each office at which deposits are accepted; and (2) delivers a notice reciting such new or increased charge to each depositor who has a deposit account which will be affected by such new or increased charge and for which such financial institution normally renders a periodic statement of account, which notice of new or increased charge shall be delivered (A) at least thirty days prior to such new or increased charge if any such periodic statement is normally rendered monthly or more frequently, or (B) no later than delivery of the next subsequent periodic statement after such new or increased charge if any such periodic statement is normally rendered less frequently than monthly.

(P.A. 79-433, S. 6, 11; P.A. 81-261, S. 5.)

History: P.A. 79-433 effective July 1, 1980; P.A. 81-261 rephrased certain parts of the section and established time periods for the delivery of a notice reciting new or increased charges depending upon the frequency with which the periodic statement is rendered to the depositor.

Sec. 36-27g. Changes in computation of interest or interest rate. Notice. (a) No financial institution, other than a credit union or federal credit union, shall change its method of computing interest in such manner as to reduce the effective annual percentage yield on any savings account from that recited in the current schedule of interest, unless the financial institution: (1) At least thirty days prior to such change, posts a notice reciting such reduction adjacent to, or incorporates such notice in, the current schedule of interest posted in each office at which deposits are accepted; and (2) delivers a notice reciting such reduction to each depositor who has a deposit account which will be affected by such reduction and for which such financial institution normally renders a periodic statement of account, which notice of reduction shall be delivered (A) at least thirty days prior to such reduction if any such periodic statement is normally rendered monthly or more frequently, or (B) no later than delivery of the next subsequent periodic statement after such reduction if any such periodic statement is normally rendered less frequently than monthly.

(b) No financial institution, other than a credit union or federal credit union, shall reduce the simple interest rate and therefore the effective annual percentage yield paid on any savings account from that recited in the current schedule of interest, unless: (1) Within fifteen days after such change, such financial institution posts a notice reciting such reduction in simple interest rate and effective annual yield adjacent to, or incorporates such notice in, the current schedule of interest posted in each office at which deposits are accepted; and (2) such financial institution delivers a notice reciting such reduction in simple interest rate and effective annual percentage yield to each depositor who has a savings account which will be affected by such reduction and for which such financial institution normally renders a periodic statement of account, which notice of reduction shall be delivered no later than delivery of the next subsequent periodic statement, if any, after such reduction.

(c) A financial institution may, without notice, change its method of computing interest in such manner as to increase its effective annual percentage yield or may increase the simple interest rate, not to exceed any maximum set by law, and therefore the effective annual percentage yield paid on any deposit account from that recited in the current schedule of interest.

(P.A. 79-433, S. 7, 11; P.A. 81-261, S. 6.)

History: P.A. 79-433 effective July 1, 1980; P.A. 81-261 rephrased certain parts of the section, amended Subsec. (a) to establish time periods for the delivery of a notice reciting a reduction in interest due to a change in computation method depending upon the frequency with which the periodic statement is rendered to the depositor, and amended Subsec. (b) to require that a financial institution which reduces the simple interest rate deliver to each depositor a notice of reduction no later than delivery of the next subsequent periodic statement after such reduction.

Sec. 36-27h. Enforcement powers of commissioner. If the commissioner finds that a financial institution is violating the provisions of this chapter, he may order such institution to: (1) Cease its unlawful practices; and (2) make restitution to any depositor for any unlawful deposit account charge or overcharge imposed on, or any interest unlawfully withheld from, such depositor.

(P.A. 79-433, S. 8, 11.)

History: P.A. 79-433 effective July 1, 1980.

Sec. 36-27i. Exceptions. Waivers. Notwithstanding any other provision of this chapter:

(a) The provisions of this chapter shall not apply to any time account containing one hundred thousand dollars or more.

(b) The deposit contract, schedule of interest and schedule of deposit account charges may exclude, and the provisions of this chapter do not apply to, any disclosures which are provided to a depositor in accordance with any state or federal law other than this chapter.

(c) For any deposit account which has more than one depositor, a financial institution need not deliver the deposit contract, schedules and notices, when such delivery is required by this chapter, to more than one of the depositors.

(d) At such time as any financial institution is authorized by law to accept a time deposit, the simple interest rate of which may vary during the term of such deposit, or at such time as interest rate ceilings on any type of savings deposit are no longer provided by law or are changing with sufficient frequency to justify, in the opinion of the commissioner, invoking the provisions of this subsection, the commissioner may issue an order waiving compliance with any or all of the provisions of this chapter by any one or more of such financial institutions with regard to such accounts for such period of time as he may designate if, in his opinion, economic or competitive conditions are such that compliance with such provisions would be detrimental to depositors and other creditors of such institutions. For the purposes of this subsection, "depositors" means persons having deposits in financial institutions.

(P.A. 81-261, S. 7.)

Sec. 36-27j. Compliance. A financial institution shall be in compliance with the provisions of this chapter if it complies with all of the provisions of sections 36-27b to 36-27g, inclusive, and section 36-27i prior to October 1, 1981.

(P.A. 81-261, S. 8, 9.)

PROTECTION FROM MISLEADING INFORMATION

Senator **Dodd**. Thank you very much, Howard, and I commend you for your testimony.

I certainly appreciate your support of S. 1507 and I appreciate your view as stated as well, that your job is not just to protect the funds consumers place in banks, but if I can quote you, you say, "Of equal importance is the protection from misleading information which might jeopardize these funds or the confidence that consumers should have when placing their money in savings accounts," and I agree with you on that as well.

Mr. **Brown**. Thank you, Senator.

Senator **Dodd**. I don't have many questions, but I don't know if you had a chance to take a look at our charts here. I've cited a couple of examples where that kind of information can be misleading. Have you had a chance to?

Mr. **Brown**. Yes, I have, Senator.

Senator **Dodd**. In Connecticut, how do our Connecticut statutes, how would they have dealt with these two situations?

Mr. **Brown**. Well, what is really revealing here is the manner in which the terms of the payment of rates or the accumulation of rates can differ so drastically. The main issue, adequate and full disclosure, and where there is full disclosure the consumers ostensibly will make an informed choice.

The problem has been where rates are not disclosed or where minimum balances are required for the customer to avail themselves of the benefits that are highly advertised and those are not disclosed, and that has been the main problem.

Senator **Dodd**. So our law requires that kind of full disclosure.

Mr. **Brown**. Our law would require full disclosure of those terms and it would leave it pretty much up to the consumer to make an informed choice.

Senator **Dodd**. I wonder if you have run across depository institutions that use the so-called investable balance method? Are you familiar with that?

Mr. **Brown**. I'm familiar with it. I have not really studied that issue specifically.

Senator **Dodd**. Basically what it is is consumers get interest on about 88 percent, as I understand it, of their deposits, an amount that would reflect of course about a 12-percent reduction for reserves.

What have we done about that in Connecticut?

Mr. **Brown**. I don't know that we have really addressed that issue, Senator. As I indicated, our law goes back to 1979. There are certain features within S. 1507 that I think we could incorporate into our State law. I think our State law would benefit from some of the issues raised by this proposed legislation.

Senator **Dodd**. Thank you very much.

Senator Chafee.

Senator **Chafee**. Thank you, Mr. Chairman.

Just out of curiosity, Connecticut has been pretty vigorous in this going way back to 1981. Why do you figure that they haven't picked up on the certificates of deposit for regulation, or I think disclosure is a better word?

Mr. **Brown**. Well, for one thing, Senator Chafee, the certificates of deposit have not been readily available to the average consumer because of the——

Senator **Chafee**. Yes, I appreciate that, and you mentioned that in your statement, but they certainly have been available in the last 5 years, wouldn't you say?

Mr. **Brown**. I would. Yes, I would say so.

Senator **Chafee**. I was just curious that Connecticut, which is aggressive in these areas, why the Connecticut legislators, since they enacted this in 1979, haven't said, certificates of deposit are now available in relatively modest denominations and let's get in and require disclosure there, too. Why hasn't your department, for example, proposed it?

Mr. **Brown**. Well, we do require disclosure, Senator, and I believe that's one of the key protections that has not led to abuse in the area which you cite.

My department through overseeing that adequate disclosure is made does effectively deal with that area, and we deal with it in a manner other than by proposing legislation, as you point out, but nevertheless I feel that we deal with it effectively. There has been no ground swell in Connecticut as a result of substantial or significant abuses in that area. If they do come to light, then I will certainly propose legislation to address that issue.

Senator **Chafee**. Do you support the mutual fund language in this legislation?

Mr. **Brown**. Yes, Senator, I do.

Senator **Chafee**. Do we get into a problem in any way where we've got too many cooks stirring the broth by, for example, the FDIC addressing the advertising requirements, as you mentioned in your testimony, and then the SEC, for example, in other sections. What about that? I'm for it. I think that it's a good piece of legislation and I think the disclosure is good. I'm just curious as to whether we're getting into areas that are already adequately covered.

Mr. **Brown**. Well, Senator, ideally I would love to see a uniform piece of legislation that applies functionally, and by that I mean with any instrument that the consumer decides or chooses to place savings into, that there would be uniform disclosure requirements that would apply to those instruments.

As you know, several instruments and products available to the consumers are more readily available now which were relegated to investment instruments years ago, and historically I suppose that's the reason why the SEC has been the primary regulatory or agency to deal with the area of the prospectuses, the contents of it, the advertising of mutual funds and the like.

Now that those products are more readily available to the average consumer they are being handled by various subsidiaries of banks and banks themselves in certain instances. Those products are now finding their way into the hands of the average consumer which gets into the FDIC's area of jurisdiction.

So as a practical matter I think we will see some of the crossing into other regulators' turfs, so to speak. I think that's an evil that perhaps we'll have to put up with until there is a broader study done and the result I would hope would be legislation that would apply across the board to each type of instrument where the consumer treats it as a savings vehicle.

METHOD OF NOTIFYING VIOLATORS

Senator **Chafee**. Let me ask you this. In Connecticut, since you wrote this law in 1979 and amended it in 1981, have you taken any action and, if so, what kind of action did you take? If some savings and loan puts an advertisement in a newspaper saying this is the interest rate and doesn't comply with your law; do you have fines? How do you handle it?

Mr. **Brown**. Well, Senator, initially a telephone call is made to the CEO of that particular institution.

Senator **Chafee**. When you spot the ad in the newspaper?

Mr. **Brown**. Yes, sir.

Senator **Chafee**. I see.

Mr. **Brown**. The telephone call is made and the ad is snatched out of the media. If it's determined that the ad is misleading, and not only misleading, but there may be some fraudulent intent to mislead the consumers, there are actions that can be brought against the parties using those tactics. It could be anywhere from an administrative fine to the lifting of a license.

Senator **Chafee**. Do you find that usually the telephone call suffices?

Mr. **Brown**. Yes, it does, Senator. In the preponderance of the cases the telephone call from me has been sufficient.

Senator **Chafee**. To put it the other way around, have you ever had to go beyond that in your experience?

Mr. **Brown**. Yes, I have, and in that instance it was a legitimate difference of opinion as to whether or not an advertisement was not reasonably calculated to state a truthful rate. We did have further discussions on that particular issue, and it was resolved in the favor of the Department of Banking. That particular institution relented and withdrew the advertisement.

Senator **Chafee**. I see. So you've never had to go to a fine?

Mr. **Brown**. No, Senator, I have not.

Senator **Chafee**. Well, I think that's the way to settle these things. Who is the enforcer of this?

Senator **Dodd**. The phone call or the fine? [Laughter.]

Senator **Chafee**. Either. The Federal Reserve would be the——

Senator **Dodd**. Yes, correct, and they are also the ones who would.

Senator **Chafee**. Is there anything here to suggest that the warning is the first step to take?

Senator **Dodd**. Let me check. Well, you have warnings I guess, and I think in some areas we've had an immigration law.

Senator **Chafee**. Well, that's fine.

Thank you very much, Mr. Brown.

Mr. **Brown**. Thank you, Senator.

Senator **Dodd**. Howard, thank you very much for being here. We appreciate your testimony.

There may be some additional questions from other members which we can submit to you in writing, but we are grateful to you for coming down.

Mr. **Brown**. Thank you very much, Mr. Chairman.

Senator **Dodd**. Senator Heinz, as many of you know, is a cosponsor of this legislation as well.

Our next panel of witnesses includes Theo Pitt, vice chairman of the U.S. League of Savings Institutions; Alan Fox, legislative representative, Consumer Federation of America; Jack Shipman, executive vice president, Liberty National Bank and Trust Co., Louisville, KY, representing the American Bankers Association; and David Silver, president of the Investment Company Institute.

We thank all four of you for being here, and I gather that you have already been asked to try and—well, first of all, I'll tell you that any prepared statements you have will be incorporated in full as if read as part of this record this afternoon, and that I would urge you to try and keep your remarks down and paraphrase your statements.

I should tell you there is one committee chairman, and my colleague from Rhode Island I think knows who it is, but he has a rule that he sends out to witnesses that if you can't come in and talk extemporaneously about the subject, then don't appear. [Laughter.]

And he says he eliminates about 50 percent of his potential witnesses that way. [Laughter.]

Now we haven't moved to that kind of a proposal and obviously it wouldn't be necessary with this panel given your knowledge of these issues, but——

Senator **Chafee**. Mr. Chairman, if I could interrupt one moment.

Senator **Dodd**. Certainly you can.

Senator **Chafee**. Unfortunately, I have a 3 o'clock engagement that I have to attend to, and I would ask, one, if I could put my statement into the record.

Senator **Dodd**. Certainly.

Senator **Chafee**. And, two, I would like to join you as a cosponsor of this legislation.

And, three, I will read over your statements and look forward to hearing about your responses to the questions.

Thank you.

Senator **Dodd**. The statement will be included in the record, I thank you for the cosponsorship and get ready for the questions when they come. [Laughter.]

Why don't you begin, Mr. Pitt, and I'll move down in the order that I introduced you and then have some questions for you.

STATEMENT OF THEO PITT, JR., VICE CHAIRMAN, U.S. LEAGUE OF SAVINGS INSTITUTIONS

Mr. **Pitt**. Thank you, Chairman Dodd, and members of the subcommittee.

I'm Theo Pitt, Jr., and I'm president and chief executive officer of Pioneer Savings Bank in Rocky Mount, NC, I appear before you today as vice chairman of the U.S. League of Savings Institutions.

The U.S. League is generally supportive of the efforts to present interest rate information to the general public in clear and understandable terms. We believe that all depositories should be subject to reasonable disclosure requirements in print advertising.

S. 1507's basic disclosure provisions are duplicative in large part of the advertising rules which have long been applied to FSLIC insured institutions, and we have no objection to codifying these rules.

It is our strong belief that in the interest of competitive fairness the scope of the Truth in Savings bill as passed by the House is too limited. Specifically, Mr. Chairman, the coverage of this important bill should extend to money market mutual funds, insurance company variable annuities, and similar competitors for personal and household savings. We welcome Chairman Proxmire's recognition of this omission in his remarks accompanying the introduction of S. 1507.

Procedural considerations are not a barrier here. Thus, we look to this subcommittee and your parent Banking Committee to improve this legislation in that regard. There is every justification for extending the coverage of truth in savings requirements to money market mutual funds and other nondepository savings-like products.

From the saver or investor's perspective these products possess many of the traits and characteristics of a deposit account at a bank, thrift or credit union wherein money can be freely deposited and withdrawn and check writing privileges are commonly available.

I have no problem with competing with money funds for the saver's dollar, but I do have problems competing where the rules are not the same and where the rules of the game favor the money funds, which is precisely what is happening and will continue to happen if those funds are not brought under the provisions of S. 1507.

The existing regulations of the Federal Home Loan Bank Board require numerous disclosures in advertising. For instance, we disclose the annual rate of simple interest and the annual percentage yield.

The Securities and Exchange Commission has no comparable advertising requirements in their current rules. But, we understand there has been a proposal pending since last September to standardize the computation of short-term mutual fund performance claims and to make certain risk disclosures.

However, some of the Commissioners have expressed publicly their reservations about proceeding to final rule-making even in the areas addressed by last year's proposed amendment. Additionally, there seems to be virtually no uniformity in the advertising of these funds and so I urge this subcommittee to include money funds and similar nondepository products under the coverage of S. 1507.

As a final matter, the U.S. League supports the language in your bill requiring that the full amount of principal be applied to the calculation of interest on interest-bearing accounts. To my knowledge, no savings institution has adopted the investable balance or reserves adjusted practice of computing interest, nor does the U.S. League condone such practices.

Savers are entitled to the full return on the amounts they deposit, and your bill will assure that result.

Thank you, Mr. Chairman and the members of this committee for the opportunity to present the views of the U.S. League. I'll be happy to try to answer any questions you may have.

Senator **Dodd**. Thank you, Mr. Pitt, very much.

[The complete prepared statement of Theo Pitt, Jr., follows:]

STATEMENT OF
THE U.S. LEAGUE OF SAVINGS INSTITUTIONS

Presented By
THEO PITT JR., VICE CHAIRMAN

Thank you, Chairman Dodd, and members of this Subcommittee. I am Theo Pitt Jr., and I am President and Chief Executive Officer of Pioneer Savings Bank of Rocky Mount, North Carolina. I appear before you today in my capacity as Vice Chairman of the U.S. League of Savings Institutions*.

I would say at the outset, Mr. Chairman, that the U.S. League is generally supportive of efforts to present interest rate information to the general public in clear and understandable terms. We believe that all depositories should be subject to reasonable disclosure requirements in print advertising. (It is our understanding that the Federal Financial Institutions Examinations Council has an ongoing project in this area.)

The legislation which you are considering today, S.1507, has been approved as H.R.176 by the House of Representatives. Its basic disclosure provisions are duplicative in large part of the advertising rules which have long applied to FSLIC-insured institutions. We have no objection to codifying those rules.

It is our strong belief however, in the interest of competitive fairness, that the scope of H.R.176 as passed by the House is too limited. Specifically, Mr. Chairman, the coverage of this important bill should extend to money market mutual funds, insurance company variable annuities, and similar competitors for personal and household savings. We welcome Chairman Proxmire's recognition of this omission in his introductory remarks accompanying the introduction of S.1507 in the July 21, 1987 Congressional Record.

I am aware that the exclusion of money market mutual funds by the House was more a recognition of procedural realities than a statement by that body that money funds should for some reason be excluded from coverage. Those procedural considerations are not a barrier here, since your distinguished full Committee has jurisdiction over securities matters as well as over depository institutions. Thus, we look to this Subcommittee and your parent Banking Committee to improve this legislation in that regard before sending it along in the process toward enactment.

---

* The U.S. League of Savings Institutions serves the more than 3,400 member institutions which make up the $1.2 trillion savings association and savings bank businesses. U.S. League membership includes all types of institutions -- federal and state-chartered, stock and mutual. The principal officers include: Joe C. Morris, Chairman, Emporia, Kansas; Theo H. Pitt, Vice Chairman, Rocky Mount, North Carolina; William B. O'Connell, President, Chicago, Illinois; and Phil Gasteyer, Executive Vice President and Director of Washington Operations. U.S. League headquarters are at 111 East Wacker Drive, Chicago, Illinois 60601. The Washington Office is located at 1709 New York Avenue N.W., Washington, D.C. 20006. Telephone: (202) 637-8900.

There is every justification for extending the coverage of Truth in Savings requirements to money market mutual funds and other non-depository savings-like products. Since their introduction in the financial services marketplace in the 1970s they have had moments of great popularity as savings instruments.

As an example, money market mutual funds grew from $10.9 billion in 1978 to $232 billion in November of 1982 -- an increase of more than twentyfold. As of March 30 of this year, money market mutual funds had deposits totalling $234.2 billion. By contrast, commercial banks had $978.8 billion in small time and savings deposits on March 30, while our institutions had $733.7 billion.

Money market mutual funds actually have surpassed the deposit base of mutual savings banks and credit unions. Mutual savings banks had deposits of $132.8 billion on March 30 while credit unions recorded deposits on that date of $147.1 billion. To put it another way, money market mutual fund deposits today nearly match in size all mutual savings bank and credit union deposits combined.

Bear in mind that the money market mutual fund carries with it from the saver/investor's perspective many of the traits and characteristics of a deposit account at a bank or a thrift or a

credit union. Money can be freely deposited and withdrawn, and check-writing privileges are commonly available. The growth of money funds has not been the result of new discretionary savings; that growth is merely the result of disintermediation from traditional depositories to these new savings-like instruments.

Now, I have no problem in competing with money funds for the saver's dollar. But I could well have problems competing if the rules of the game are changed in such a way as to favor the money funds, which is precisely what will happen if those funds are not brought under the provisions of S.1507.

Existing regulations of the Federal Home Loan Bank Board require numerous disclosures in advertising (12 CFR 526.2). We are required to disclose the annual rate of simple interest, the percentage yields based upon one year and percentage yields based upon more than one year. If a stated rate is payable only on savings accounts that meet time or amount requirements, we must clearly and conspicuously say so. If there is a penalty for early withdrawal, we are required by regulation to forewarn our depositors, just as we must make known any fees that might be associated with any account.

The Securities and Exchange Commission, which regulates investment company products, has no comparable advertising requirements in their current rules. We understand that there has been a proposal pending since last September to standardize the computation of mutual fund performance claims and make certain risk disclosures, but it is also our understanding that no final rules are anticipated before year's end and several of the Commissioners have expressed publicly their reservations about proceeding to final rule-making in even these areas. Under present rules, so long as advertising states that a prospectus is available, it meets the requirements of the Securities Acts.

Does this advertising explain to the prospective client that their investments in money market funds are essentially equity investments? Does the advertising explain that, because his or hers is an equity interest, the investor has no absolute right to a return of principal? These types of questions are not disclosed.

In practice, the biggest and boldest type in money market fund advertising is reserved for the claims of percentage yield, claims which usually carry an asterisk referring to the fine print at the bottom of the advertising. On reading the fine print, the reader learns that the advertised rate is usually based on past performance, and this is often explained in complex terms.

Finally, there seems to be virtually no uniformity in the advertising of these funds. One fund will include in its fine print the disclaimer that the yield might vary with changes in interest income, in public offering price, the frequency of payout and the amount invested. Another fund's fine print might provide a formula for calculating the percentage yield by dividing the last dividend by the average price per share. Yet another fund's fine print might state that the yield assumes the reinvestment of all dividends and capital gains. In other words, there is no uniformity of the sort we are required by Federal Home Loan Bank Board regulations to demonstrate.

Clearly, Mr. Chairman, the money funds and insurance company variable annuity products are focusing on the very same markets as our savings institutions, commercial banks and credit unions. If the purpose of this legislation is to make decisions easier for the investing and saving public that comprise that market, then these competitors should be required to adhere to advertising guidelines comparable to our own. I urge this Subcommittee to include money funds and similar non-depository products under the coverage of S. 1507.

Senator DODD. Mr. Fox, we welcome you back to the committee and appreciate your being here this afternoon.

STATEMENT OF ALAN FOX, LEGISLATIVE REPRESENTATIVE, CONSUMER FEDERATION OF AMERICA

Mr. FOX. Thank you, Mr. Chairman.

I appreciate the opportunity to appear here today on S. 1507 which represents one of the highest priorities of the Consumer Federation of America, and I want to indicate that I'm appearing as well on behalf of Consumers Union and the American Association of Retired Persons which have joined in developing the written statement that we've submitted.

The market for deposit accounts ought to operate as a free market. Prices, whether you're looking at fees or interest rates, are completely deregulated today. There is not free entry into the market, but there is certainly a large number of providers of deposit or deposit-like services in most markets around the country.

But in fact the market does not operate well for consumers and it does not operate well because basic information on pricing is not routinely available to consumers. When it is available it is rarely comprehensible to the average consumer.

BANK AND THRIFT ACCOUNT FEES

The Consumer Federation has conducted four annual surveys of bank and thrift account fees in markets around the country, and in every one of those surveys, which have involved 600 or 700 interviews or questionnaires or attempts to get information from various institutions, what we found is that the information is not available at the branch level where the average consumer will try to get the information or it's given inconsistently by branch personnel who have no written material and are not properly trained in providing information orally or it's incomplete and often it's even erroneous and different interviews with different people at the same institution hours apart will produce different answers and sometimes neither answer is correct.

Even when the information is accurate, it's rare that consumers are able to compare the information. We looked at brochures from about 70 or 80 different banks and thrifts around the country this year and found over 50 different phrases used to describe the balance method on which interest is calculated at those institutions. Not all the phrases obviously met different things, but there is no way that a consumer can look at those different terms and make head or tail of them.

No market can operate efficiently if consumers can't acquire enough information to reward providers of best values, to penalize deceptive behavior and simply to influence market behavior through rational purchasing decisions. That's the situation we have today with the market for deposit accounts and similar accounts.

Why is this legislation needed? I think we have the examples in this room and we've submitted others in our testimony. We have examples of free accounts that aren't free, accounts that have the same rate of interest and the same annual percentage yield, but somehow still pay consumers different amounts of interest in dollars and cents, and of course what matters to consumers is not what the number is with the percentage figure after it, but what the dollars and cents outcome of holding that account is.

We have found disclosure statements that failed to disclose anything at all that has to do with pricing, fuzzy language that obscures important terms, we've found different banks using different phrases to mean the same thing and we've even found different banks using the same phrases to mean different things.

ANALYZING DEPOSIT ACCOUNTS

The most clear-cut example that we've encountered in the last few years of analyzing deposit accounts, the most clear-cut example of an attempt to obscure terminology and deny consumers the ability simply to understand what's going on is the example, Mr. Chairman, that you've pointed out, the so-called investable balance technique, and it goes by a variety of other names and sometimes in some disclosures it doesn't have any name at all.

That's a calculation technique that's used to determine how much interest consumers will receive on deposit accounts. Well, you'll hear a lot of talk about how the technique was developed, references to legally required reserves and a lot of other things that do nothing more than obscure the issue.

What the investable balance technique is is no more than a device to allow a bank that is paying 4.4 percent interest to claim it's paying 5 percent interest. Now that's something that is simply out of bounds and ought to be out of bounds and is out of bounds everywhere it seems except in the banking industry and in the industry of providing deposit accounts.

We don't let supermarkets claim that they are selling consumers a pound when they are only selling them 14 ounces. That's something that is beyond dispute. Nobody tries to argue that that's something that the free market or product design or open competition requires. It's a question of elemental fairness and basic honesty, and it's something that is properly taken care of in this legislation. Congress should ensure that this technique has no further place in the marketplace.

Thank you.

Senator DODD. Thank you very much for your testimony.

[The complete prepared statement of Alan Fox follows:]

Other Concerns

As a final matter, the U.S. League supports the language of the House-passed bill (included as Sec. 7(a) in S.1507) requiring that the full amount of principal be applied to the calculation of interest on interest-bearing accounts. This provision was added in House Committee to address the practice apparently used by some commercial banks of calculating interest on the "investable" or "reserves adjusted" balance, rather than the full amount deposited by the savings customer.

Since the enactment of universal reserves in the Monetary Control Act of 1980 (P.L.96-842), savings institutions have been subjected to the sterile reserves requirements of the Federal Reserve System. To my knowledge, however, no savings institutions have adopted the "investable" or "reserves adjusted" balance practice -- nor does the U.S. League condone such practices. Savers are entitled to the full return on the amounts they deposit and Sec.7(a) will assure that result.

Thank you, Mr. Chairman and Members of this Subcommittee, for this opportunity to present the views of the U.S. League. I will try to answer any questions you might have.

- # -

CFA
Consumer Federation of America

STATEMENT ON

"S. 1507: TRUTH IN SAVINGS"

BY

ALAN FOX
LEGISLATIVE REPRESENTATIVE
CONSUMER FEDERATION OF AMERICA

ON BEHALF OF:
CONSUMER FEDERATION OF AMERICA
AMERICAN ASSOCIATION OF RETIRED PERSONS
CONSUMERS UNION

BEFORE THE
SUBCOMMITTEE ON CONSUMER AFFAIRS

SENATE COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS
HON. CHRISTOPHER J. DODD, CHAIRMAN

August 5, 1987

1424 16th Street, N.W., Suite 604 • Washington, D.C. 20036 • (202) 387-6121

My name is Alan Fox. I am Legislative Representative for Consumer Federation of America (CFA), which consists of over 230 local, state and national consumer, senior citizen, rural, cooperative and labor organizations that together have over 50 million members. CFA has, since 1968, represented these organizations before Congress and federal regulatory agencies on a wide variety of matters of concern to consumers.

I appreciate very much the opportunity to testify on S. 1507, the "Truth in Savings Act," which embodies the principles of one of CFA's highest priorities, that of full, complete, comparable disclosure of all of the elements of financial services pricing.

This statement is presented on behalf of CFA and two other organizations that share CFA's commitment to this legislation:

The American Association of Retired Persons (AARP), with more than 25 million members, is the nation's largest organization of Americans 50 years of age and older. The nonprofit, nonpartisan organization offers a wide range of membership benefits, legislative representation and the federal and state level, and educational and community service programs carried out by a network of volunteers and local chapters.

Consumers Union (CU), a nonprofit membership organization that provides information, education, and counsel about goods and services and the management of family income. CU publishes Consumer Reports, with a circulation of approximately 3 million, which reports on its own product testing as well as on a variety of other issues that affect consumer welfare.

INFORMATION NEEDED FOR MARKET TO FUNCTION

Adequate information is essential to a fully functioning and efficient market. In the past, strict regulation of deposit accounts presented consumers comparing different accounts with a relatively straightforward task. Account terms varied little and competition between depository institutions and other providers of similar services was limited.

Today, the terms, conditions and prices of deposit accounts are almost completely unregulated, and consumers are faced with a widening variety of deposit services offered by a widening variety of institutions. This transformation of the market for financial services has benefited those consumers with adequate resources to take advantage of their new options. For most consumers, however, the expansion of options has not been matched with the expansion of information necessary to evaluate options and make informed choices.

A market cannot operate efficiently if buyers of services are routinely unable to determine the prices and compare the value of competing services. Consumers today have a great deal of difficulty acquiring information, and greater difficulty comparing what information is available from competing depository institutions. The result is an inefficient market that fails to reward providers of the best values, fails to penalize deceptive behavior, and fails to allow consumers to influence market behavior through rational purchasing decisions.

COMPARING CONSUMER ACCOUNTS

A consumer who attempts to find the best place to keep a deposit account or who tries to evaluate an advertisement for such an account has an increasingly difficult task. Simply learning which account has a higher interest rate is not sufficient. The consumer must also know the basis of compounding, whether the interest is paid on an average or low balance, any minimum balance required to receive interest, and how the minimum balance is calculated. That task is further complicated by the difficulties of comparing time deposits of varying maturities and by accounts that offer different rates of interest on different amounts or over the life of the deposit, or that vary the rate of interest to reflect market changes.

But even that is only half the job -- the income half. Service fees are taking a bigger and bigger chunk of consumers' dollars, and the types of fees charged are proliferating as well. The consumer trying to compare accounts must ask about monthly fees, per item fees, ATM fees, bounced check charges, returned deposit charges, and when those fees will be assessed, a factor that may depend on an average balance, a current balance, a number of transactions per month, or any of several combinations of factors.

As deposit accounts have been deregulated and the types of fees charged have expanded, this job has become far more difficult. Consumers have more accounts to compare and more factors to look at in each account. Financial institutions have tended to compete by advertising the rosiest picture possible, for example the interest rate paid in a short, introductory period of only a few days. Financial institutions have emphasized income to consumers in their advertisements and disclosures, while leaving consumers to find out about costs on their own. Consumer organizations that have attempted to provide a full picture through fee surveys have consistently come away frustrated by lack of cooperation and lack of accurate information.

TWO PARTS TO ADEQUATE ACCOUNT DISCLOSURE

Two types of disclosures are needed to allow consumers to compare account offerings: Accurate and uniform disclosure of interest income on deposit accounts, and disclosure of all the potential costs of consumer accounts. Legislation should be drawn to provide consumers with the full picture -- accurate, concise, comparable information on the costs and benefits of deposit accounts.

INCOME DISCLOSURE

We recommend that Truth in Savings legislation require depository institutions to make a standardized disclosure of several yield-related terms. These should include the annual rate of simple interest (ARSI), the method of compounding, and, most importantly, the annual percentage yield (APY), which should be uniformly defined to reflect the application of the annual rate of simple interest and the compounding period over a 365-day year.

The APY disclosure generally assumes both that a single rate will apply for a full year and that funds will be left on deposit for a full year. The legislation should require a tailored APY disclosure in special cases where these assumptions are not appropriate. These include:

- Time deposits of less than one year, where an APY assumes that the deposit may be rolled over at the same rate.

- Accounts with variable interest rates linked to market indices or, more commonly, varied periodically according to the judgment of bank managers.

- Introductory or "teaser" rates that apply for a short time, after which a lower or a variable rate takes effect.

- "Bonus" rates that take effect only after an amount has been on deposit for a fixed time.

- Tiered rate accounts, on which different rates of interest are paid on different balances.

- Combinations of any of the above, such as tiered rates where one or more tiers pay variable rates or variable rate accounts with introductory teaser rates.

As a general rule, disclosures for accounts with features such as these must include enough information for a consumer to fully understand these features, as well as related information such as balance requirements necessary to receive a particular rate of interest.

THE NEED FOR A STANDARDIZED BALANCE CALCULATION METHOD

As consumer organizations have stressed for years, different methods of calculating the balance on which interest is paid have a significant effect on accounts' yield, and effect which is not, and cannot be, incorporated into standard yield measurements such as the APY.

These differences were clearly illustrated in the February 1975 Consumer Reports (see attachment). Four passbook savings accounts were maintained for six months, with identical deposits and withdrawals. Each account had a 6% annual rate, compounded quarterly. Each would thus be entitled to state an annual yield of 6.14%. But the actual amount a consumer would receive in interest varied from $44.93 to $75.38.

Most consumers assume that interest is paid on a day-of-deposit to day-of-withdrawal basis or on a daily basis. But as the Consumer Reports article indicates, interest may be paid on a variety of other balance calculation methods, including a low balance method, where interest is paid only on the lowest balance in the account on any one day of the month. The effect of this technique may be to eliminate interest earnings altogether.

According to the American Bankers Association's 1985 Retail Deposit Services Report, a wide variety of methods to calculate balances are still in use. Methods identified include:

Day of deposit to day of withdrawal
Day of deposit to end of interest period
Low balance for interest period
Low balance for month
Average balance for month
Average balance for interest period

Other unidentified methods were not included in the report's tables.

When different balance methods are used, comparison between accounts becomes impossible. It is not enough to know that two accounts each have yields of 5.65%. The question consumers need answered is "5.65% of what?" Consumers receive dollars, not percentage points, and the account that pays the most is the one that pays the most dollars, regardless of the percentage rate.

Simple disclosure will not remedy the problems caused by depository institutions' use of varying balance calculation methods. First, our repeated inquiries have indicated that few members of the banking industry itself understand and can clearly articulate the differences between the methods in use now. This bodes poorly for the ability of consumers to understand balance calculation method disclosures. Second, even if consumers clearly understood these differences, the would still be ill-equipped to calculate the comparative values of accounts with different APYs and differing balance calculation methods.

The only clear solution to this important problem is a legal requirement mandating use of a single method for calculating all balances used to determine interest payments on deposit accounts. If balance calculation methods are not standardized, consumers will not be able to use the other account disclosures to accurately compare accounts.

By deregulating interest rates on deposit accounts, Congress made a policy decision to promote competition in consumer deposit services. However, true competition will continue to be impaired until consumers are given the means to accurately compare among competing product claims. Standardization of balance calculation methods is a prerequisite to comparison shopping. We do not, in the name of the "free market," allow retailers to define weights and measures any way they wish, because we recognize that variations in weights and measures do not promote but impede true competition. Balance calculation standardization would serve as the true weights and measures law of financial services.

"INVESTABLE BALANCE:" BANKS' VERSION OF SHORTWEIGHTING

The "investable balance" method illustrates the willingness of many banks to go to great lengths to confuse and shortchange consumers. CFA discovered and publicized this deceptive method earlier this year, and the American Bankers Association later determined that about one commercial bank in seven uses this technique on at least some of its consumer accounts.

Under the "investable balance" method, banks pay the disclosed rate of interest only on a portion of a consumer's account -- usually 88% of the balance. The justification given for this practice is that banks are obligated by the Federal Reserve System to place an amount equal to about 12% of their total interest-bearing demand deposits in reserves. Some banks have decided that they should not pay depositors interest on these amounts, either.

We reviewed materials from several banks that use this practice. Most did not state what proportion would be deducted from the balance, leaving the depositor to guess what was meant by the phrase "investable balance." All inaccurately implied, by reference to legally-required reserves, that the withholding of interest was also legally required.

The technique is the banker's equivalent of the butcher's thumb on the scale. A disclosed interest rate should mean exactly what it says, and no less. No bank should be allowed to say it pays 5.25% interest when it only pays that interest on 88% of an account. Banks should be required to reduce their claimed rate -- in this case to 4.62% -- so consumers have an accurate picture of the true value of an account.

Congress will have to require this of banks, because bank regulators will not. On June 3, 1987, CFA asked the Comptroller of the Currency to:

> (T)ell banks under your jurisdiction that interest must be calculated on the basis of the full balance in the account, and that any exclusion from the full balance must result in a proportionate adjustment of the disclosed interest rate and yield. If banks can unilaterally decide to pay interest on any portion of the balance they desire, then the annual rate of simple interest will have no meaning and consumers will be unable to determine which bank pays which rate of interest.

On July 24, 1987, Comptroller Robert Clarke responded by refusing to require national banks to adjust their stated rates of interest to reflect this balance method. The letter states:

> The practice of paying interest on the portion available to invest reflects one way that a bank uses to price its accounts. However advertisements of banks that price their accounts in such a manner must include reference to that practice. (Emphasis added)

The Comptroller's response is an admission that the interest rate and yield are not to be relied on by consumers. A "reference" in a disclosure to the "investable balance" method tells a consumer nothing. Even if the "reference" discloses that the consumer will receive interest on only 86% of the account, the consumer will have great difficulty determining which account pays more and which pays less. We would not sit still for a minute if a supermarket charged for its meat on the basis of a "14-ounce pound" -- no matter how clearly the practice was disclosed. Why should consumers be expected to put up with an "86%-balance account?"

FEES DISCLOSURE

Even full disclosure of interest yield no longer gives consumers a complete picture. Interest yield is gross, not net, income. In recent years, disclosure of account fees has become especially important in evaluating consumer accounts. Between 1979 and 1983, the Federal Reserve Board reported, fees on accounts doubled to over $10 billion a year. CFA's annual survey of account fees has revealed that these increases are continuing. Since CFA's first survey, just three years ago, we have found that the cost for moderate usage of a small NOW account has increased 42%. CFA's most recent survey, released in June of this year, confirms that these fees are continuing to increase even as the interest rates paid to consumers have begun to decline.

These surveys have also documented the fact that fees are becoming more numerous and more complex. In addition to relatively well-known fees -- monthly charges on accounts with balances below a certain minimum and bounced check charges -- fees are now charged in some instances for automatic teller machine transactions and for depositing a check that is returned for insufficient funds. Many institutions charge fees for each check written in addition to a monthly fee. And the monthly fee may be tiered depending on account balances, with as many as five different rates assessed on different balances. In some cases, fees are charged based not on the minimum balance, but on the number of transactions in a month.

Our surveys have revealed some new and imaginative ways of charging for deposit services. Some banks charge not for each automatic teller transaction but charge monthly or annually for possession of an ATM card. These charges range as high as $16 per year. One institution with a $7 monthly charge for failure to meet a balance requirement charges an additional $10 per month should the consumer desire return of cancelled checks. Several charge more for teller visits than for ATM transactions, or impose hefty monthly fees if the customer talks too often with a human teller. A number of other banks have gone beyond charging consumers for withdrawals and charge as well for each deposit.

Consumer organizations that have attempted to survey these fees have invariably found that they are unable to get accurate information from employees in branches, where consumers go to ask questions and open accounts. As Ken McEldowney, Executive Director of San Francisco Consumer Action, told an American Bankers Association conference in 1985:

> It seems clear to us that the communication of facts about prices, rates and basic bank policies has a very low priority at most banks. Even banks which publish brochures that are otherwise excellent often leave out prices. For 12 years, we have been presented with confusing, misleading and downright incorrect answers every time we tried to obtain information at the branch level.

As a result of our experiences with fee surveys and from consumers' experience with inadequate or misleading fee and interest rate information, we believe that voluntary disclosures have not and will not work. The commitment on the part of the industry is lacking.

Voluntary efforts cannot work because information must be presented in a consistent format and with consistent terminology in order to allow consumers to make informed choices. This consistency is needed because few consumers can become experts in the business of placing investments or deposits. They make such choices infrequently in a market that may change rapidly, and which is at times barely comprehensible even to those who observe it closely. Consistent terminology and consistency of disclosures cannot evolve from the market. Consistency can only be mandated by regulation or legislation. Mandated terms and formats for disclosures need not be costly to develop and should ease banks' compliance problems by providing a simple format for meeting such requirements.

THE ACCOUNT SCHEDULE

Section 4 of S. 1507, which requires maintenance by each depository institution of a written schedule of fees, charges, terms and conditions, is a key part of this legislation. Disclosure of the fees and conditions pertaining to deposit accounts is essential to rational consumer shopping and the efficient functioning of the market.

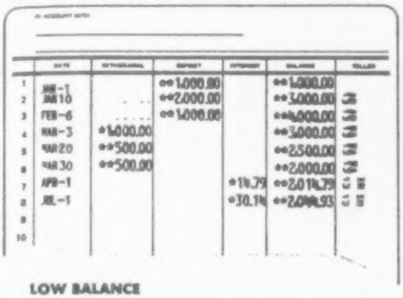
The account schedule described in Section 4 is designed to provide complete information to customers and potential customers. To be useful to consumers, the schedule must meet three general requirements:

1) It must be comprehensive. Not only must every fee be disclosed, but other relevant terms, such as balance levels, must be disclosed as well. Disclosure standards for variable rate accounts such as Money Market Deposit Accounts must be developed.

2) The terminology must be consistent. Congress should require the Federal Reserve Board to define the terms used in the schedule so consumers will have confidence that when two disclosures use the same terms they mean the same things.

These four banks all pay the same interest rate—yet interest payments range from $44.93 to $75.30.

There are many ways of computing interest, as the text of our report indicates. Here are four passbooks showing the identical deposits and withdrawals (made on the same days), with explanations of how the interest has been computed under four common methods. All four assume a six per cent interest rate and quarterly crediting and compounding.

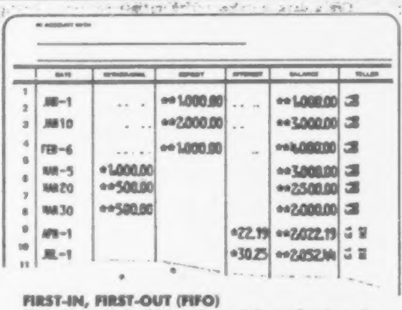


JAN-1		**1,000.00		**1,000.00
JAN10		**2,000.00		**3,000.00
FEB-6		**1,000.00		**4,000.00
MAR-3	*1,000.00			**3,000.00
MAR20	**500.00			**2,500.00
MAR30	**500.00			**2,000.00
APR-1			*14.79	**2,014.79
JUL-1			*30.14	**2,044.93

LOW BALANCE

Under this method, interest is paid only on the smallest amount of money that was in the account during the interest period. Despite a balance that reached $4000 during the first quarter, this account earned interest only on $1000—the lowest balance during that period. (There are no withdrawals during the second quarter, so the low-balance formula is not important there.) This method, which tends to discourage deposits, is the most punitive to savers. Yet 30 per cent of commercial banks still use it, according to a study last year by the American Bankers Association.

Interest: $44.93

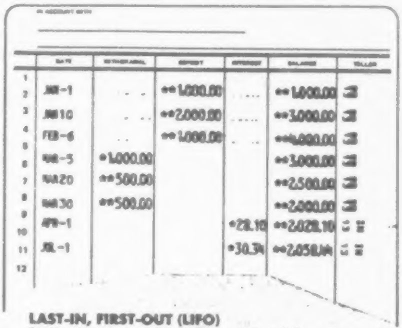


JAN-1		**1,000.00		**1,000.00
JAN10		**2,000.00		**3,000.00
FEB-6		**1,000.00		**4,000.00
MAR-5	*1,000.00			**3,000.00
MAR20	**500.00			**2,500.00
MAR30	**500.00			**2,000.00
APR-1			*22.19	**2,022.19
JUL-1			*30.25	**2,052.44

FIRST-IN, FIRST-OUT (FIFO)

With this method, withdrawals are deducted first from the starting balance of the interest period and then, if the balance isn't sufficient, from later deposits. This erodes the base on which your interest is figured and means you automatically lose interest on withdrawals from the start of the interest period rather than from the dates on which the withdrawals were actually made. Another variation of this method is to apply the first withdrawal to the first deposit, rather than to the beginning balance; this would earn $53.93. About 16 per cent of commercial banks use the FIFO methods, according to the ABA.

Interest: $52.44

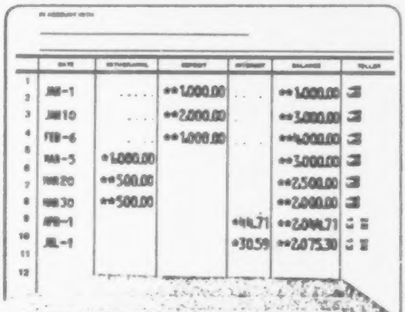


JAN-1		**1,000.00		**1,000.00
JAN10		**2,000.00		**3,000.00
FEB-6		**1,000.00		**4,000.00
MAR-5	*1,000.00			**3,000.00
MAR20	**500.00			**2,500.00
MAR30	**500.00			**2,000.00
APR-1			*28.10	**2,028.10
JUL-1			*30.34	**2,058.44

LAST-IN, FIRST-OUT (LIFO)

Under this plan, withdrawals are deducted from the most recent deposits in the quarter and then from the next most recent ones. This method, which does not penalize savers as much as the two FIFO methods, is used by about 5 per cent of commercial banks.

Interest: $58.44



JAN-1		**1,000.00		**1,000.00
JAN10		**2,000.00		**3,000.00
FEB-6		**1,000.00		**4,000.00
MAR-5	*1,000.00			**3,000.00
MAR20	**500.00			**2,500.00
MAR30	**500.00			**2,000.00
APR-1			*44.71	**2,044.71
JUL-1			*30.59	**2,075.30

DAY-OF-DEPOSIT TO DAY-OF-WITHDRAWAL

Under this arrangement, the bank pays you interest for the actual number of days the money remains in the account. This method, which is sometimes called daily interest, instant interest, or day-in day-out, is the fairest to consumers. It is used by almost 50 per cent of commercial banks and 60 per cent of insured S&Ls (there are no industry figures for savings banks). It yields the greatest return.

Interest: $75.30

3) The disclosures must be consistent in format. Disclosure forms, left to the imagination of marketing departments, have resulted in slick brochures with information buried in reams of useless text. If consumers are to use disclosures to compare accounts, the form as well as the substance of the disclosures must be consistent. A simple chart, separate from distracting text, would allow consumers to place the disclosures of two banks side-by-side and make comparisons.

CONTENTS OF THE ACCOUNT SCHEDULE

A complete disclosure schedule should include information on:

1) Minimum initial deposits
2) Minimum balances to avoid fees
3) Monthly fees
4) Per transaction charges for all types of transactions including ATM fees
5) Excess withdrawal charges
6) Bounced check charges
7) Returned deposit charges
8) Stop payment order charges
9) Balance inquiry charges
10) Account closing charges
11) Inactive account charges
12) Costs for printing checks
13) Any other fees for services routinely offered
14) Interest rate (or method of determination of interest for variable rate accounts)
15) Delayed funds availability policies
16) Non-fee requirements for opening accounts
17) Fees for check cashing by non-depositors
18) Relevant terms and conditions such as any minimum balance necessary to avoid a fee or to receive a particular rate of interest and the method used to determine the balance.

The law must ensure complete disclosure when interest rates or fees are split by time, balance, or account activity Full disclosure of every level of each such term is necessary. Special provisions are also needed for disclosures of the return on variable rate deposit accounts such as Money Market Deposit Accounts (MMDAs). At a minimum, disclosures should clearly indicate that the interest rate is variable and cannot be guaranteed; what the basis and frequency of the variation are; and consistent historical data about the performance of the account. S. 1507 contains all the factors we believe necessary to ensure consumers will receive the information they need.

ADVERTISEMENTS

Section 3 of S. 1507 specifies disclosures of interest rates and account terms in advertisements and other solicitations. These disclosures need not be as comprehensive as the full disclosures necessary in account schedules, and the disclosure requirements should only be invoked when an advertisement refers to an account's yield. While advertisements should be required

to use consistent terminology to prevent misleading or confusing consumers, it is not appropriate to require consistent formatting of information beyond what is described here. As Section 3 indicates, these requirements should only be invoked when an advertisement refers to an account's yield.

In advertising that cites yield or other interest rate information, the Annual Percentage Yield (APY) is the most important yield figure because it incorporates both the interest rate and the effect of compounding. Unlike an Annual Rate of Simple Interest (ARSI or rate) disclosure, the APY disclosure will allow consumers to compare apples with apples. Although knowledgeable consumers can derive the APY if they know both the ARSI and the frequency of compounding, most consumers cannot. Most consumers are also so unfamiliar with financial terminology and concepts that they do not know which figure is more relevant to yield when confronted with both the ARSI and APY.

CONSISTENCY OF CONTENT AND FORMAT

We cannot stress enough the necessity for both terminology and format to be consistent. If the law allows confusing or misleading terminology, or allows different providers to use the same term to mean different things, consumers will be unable to make use of the information. Consistent formats in account schedules will facilitate comparisons between accounts and will also facilitate compliance by removing design as a consideration.

The complete lack of consistency in today's advertisements was documented by Dr. Richard L. D. Morse, PhD., in a paper presented to CFA's conference on financial services in December 1986. Dr. Morse examined 23 advertisements for deposit accounts in one day's Washington Post. The advertisements used eleven different terms for the yearly or annual rate, including:

Current Rate
Rate
Annual Interest Rate
Annual Rate
Interest Rate per annum
per annum Simple Interest
Bonus Rate
APR Simple Interest
Annual Percentage Rate
Average Daily Rate
Current Yield

Nine of the advertisements contained a number with or without a percentage sign, and no additional terms.

The yield was also described with a wide variety of different terms, including:

Effective Annual Yield
Annual Yield
Yield
Annualized Yield
Current Yield
Effective Yield
Compounded Yield
Consistent Average Yield
Taxable Equivalent Yield

As Dr. Morse has repeatedly pointed out, even as seemingly straightforward a concept as a "year" can turn slippery and elusive when depository institutions calculate interest yield. In the advertisements cited, three different methods of continuous or daily compounding were used, utilizing different definitions of a year.

Consistency by its nature cannot be arrived at through voluntary efforts. If even one institution uses its own terminology, a voluntary effort has failed. When disclosures are mandated but consistency is not, behavior that is misleading or deceptive will often be rewarded by allowing dishonest providers to make their services and terms look more attractive relative to honest providers. Consistency protects those who are most willing to disclose fairly by taking away any advantages their competitors may gain through misleading disclosure.

If consistent use of terminology is not required, consumers will continue to be plagued with "disclosures" such as the statement used by some that "interest is paid on the highest balance on deposit the entire month," which only after careful scrutiny can be discovered to mean the same as "interest is paid on the lowest balance reached by the account on any one day in the month." If the law is to be useful to consumers, it must make impossible misleading terminology of this nature.

We urge requirement of a consistent format for account schedules to allow comparison among accounts. Consumers must be able not just to look at the costs of their own account, but to compare their account with competitive accounts. There are many practical barriers to switching accounts in order to take advantage of a better offer. These barriers should not be buttressed with information disclosure in a format that does not even allow a determination that the better offer exists.

Banks and other financial institutions that argue that consumers do not take advantage of currently available information fail to take into account the fact that their inconsistent disclosures have rendered practical use of those disclosures impossible. In contrast, consumer groups such as Consumer Action and Public Citizen that publish comparative information in chart form have been flooded with requests for the information, even when they must charge or require a stamped envelope.

MUTUAL FUNDS

As now written, S. 1507 applies only to accounts at depository institutions. In recent years, a variety of other institutions have begun to offer services with features similar to deposit accounts. Many of these services are intended to compete, and do compete, directly with depository institution accounts.

Mutual funds, in particular, have characteristics similar to accounts offered at depository institutions. They are offered to consumers in clear competition with depository institution accounts. With the recent introduction of bank money market deposit accounts, what once were clear lines between depository institution and securities products have become blurred.

S. 1507 should ensure full disclosure of essential terms of mutual funds in a manner as consistent as possible with the disclosures required of deposit accounts. There are important distinctions, however, between mutual funds and most depository institution accounts that must be recognized.

The most important distinction is that mutual funds advertise interest rates and yields that are purely historical in nature. While banks' interest rates are increasingly not guaranteed for any significant length of time, they more accurately reflect current and future terms than do the claims of their nondepository competitors.

As any quick perusal of mutual fund advertisements will show, there is no standardization in the time period over which historical yield data is calculated. The July, 1987 issue of Money magazine included advertisements displaying yield data for periods ranging from seven days to five years. No consumer could hope to compare these figures.

A second issue is the treatment of sales charges. Advertisements should be required to disclose the existence and amount of any sales charges, and these charges should be incorporated into yield disclosures in a consistent manner. Current advertisements do not treat sales charges consistently, and may or may not include the amount of the charge.

S. 1507 should acknowledge the competition for consumer dollars between mutual funds and depository institution accounts. At the same time, it must also reflect the current regulatory status of mutual funds. In many respects, mutual fund disclosure is already more stringent than what is called for in S. 1507. Consistent treatment of bank and mutual fund products would not only require inclusion of mutual funds in S. 1507, but would also require strengthening some current provisions of S. 1507.

Mutual fund advertisements are now subject to Securities and Exchange Commission (SEC) rules. Prospectuses, which must be provided to consumers before they may invest, contain far more disclosures than do the fee schedules proposed under S. 1507. Money market mutual funds must use a standardized calculation method to state yields, and that method requires a uniform method of determining consumers' balances. Advertisements must be submitted to the SEC for review.

Furthermore, the SEC is considering additional rules extending uniform yield disclosure to equity and income funds and improving other aspects of mutual fund disclosure. These rules were first proposed over ten months ago.

S. 1507 should recognize and encourage these actions by the SEC and it should ensure that the SEC retains authority over mutual fund disclosures. Amending S. 1507 to simply bring mutual funds under the coverage of the bill would not be in consumers' best interests.

We urge the committee to consider two proposals to ensure clear and consistent disclosure of mutual fund yields and fees. First, the SEC should be directed to issue regulations by a specific date to standardize mutual fund yield calculations, require disclosure of yield figures over consistent periods of time, and to include a clear and conspicuous table of fees in a prominent place in mutual fund prospectuses.

Second, the SEC and the Federal Reserve should be directed to consult regularly to ensure that disclosures for comparable products are consistent. The agencies should be directed to report the results of their consultations to Congress so the two Banking Committees can monitor their actions in this regard.

These steps will guarantee that mutual fund consumers will receive the information they need to compare accounts and that, to the extent possible, consumers choosing between depository institution and mutual fund offerings will be able to make informed choices, while preserving a regulatory structure that makes sense.

CONCLUSION

Accurate and comparable information about bank account terms is vital if the market is to operate efficiently. Consumers can and will use this information to discipline poor performers and reward good performers. Voluntary disclosure efforts are not working, and cannot work because they cannot produce the level of standardization of terminology or format necessary for the average consumer to use these disclosures effectively. S. 1507 provides consumers with the key disclosures they need to accurately determine the costs and benefits of deposit accounts. Coupled with badly-needed standardization of deposit account terminology and of balance calculation methodology, S. 1507 will give consumers a fighting chance in the new market for financial services.

LIST OF ATTACHMENTS

1. Consumer Reports chart showing effect of different balance methods on interest payments

2. Citibank (New York State) brochure that fails to disclose fees for failure to maintain minimum balance

3. Bank of America brochure with no information on fees

4. Columbia First Federal Savings & Loan brochure that fails to mention balance requirement and fee for savings account

5. American Security Bank brochure that fails to disclose Money Market account minimum balance requirement and fee

6. Excerpt from First Interstate Bank of Oregon brochure stating that fee and service charge information will be provided when an account is opened

7. Mutual Fund advertisements from the July 1987 Money

8. Letter to customers from First of America Bank mentioning, but not describing, initiation of "investable balance" method

9. June 3, 1987 letter from Alan Fox to Comptroller of the Currency Robert L. Clarke concerning "investable balance"

10. July 24, 1987 letter from Comptroller Clarke

Citibank Checking. A good deal, a great value.

With low minimum balance requirements that help you avoid fees, complete monthly statements, unlimited check writing and no per-check charges, Citibank's checking accounts have it all.

Add the convenience of Citicard, an interest earning option, and the bounce-proof protection of Checking Plus and you've got a checking account that works hard, so you get even more for your money.

Visit your Citibank branch today, and choose the checking account that's just right for you.

CHECKING CHOICES

	Personal Checking	NOW Checking	Citi-NOW Checking
Opening Deposit	$1.00	$1.00	$1,000.00
Interest Rate	—	5¼%	Variable
Checks Returned	Yes	Yes	No
ATM Access	Citicard—24 Hour Banking convenience at Citicard Banking Centers and Metroteller* locations throughout the state		
Special Features	No service fee if average monthly balance is $300 or more	No service fee if $1,000 in any combination of Citibank accounts	Earns interest (5¼%) even if monthly balance falls below $1,000

A world of Citi-banking benefits

From the interest-earning ability of IMRA and Passbook Plus, to the convenience of Citibank checking and cash power of Citicard, we offer more ways to better meet your everyday banking needs.

Our investment products, like CitiChoice CD's, and IRA's, help you get the most from your savings dollars. And our credit services—from home mortgages to revolving lines of credit and personal loans—allow you to choose the type of credit product that is best for you.

At Citibank, you'll find everything you need for smart, convenient banking.

Thank you for being a Citibank customer

We appreciate your business. And whenever you visit a Citibank branch, call or write, we'll try our best to give you the kind of service that means thank you.

BUFFALO AREA

409 Main at Clinton
Downtown Buffalo
(716) 849-2500

Great Arrow Plaza
Delaware & Great
Arrow Aves
Buffalo
(716) 873-4233

Transitown Plaza
Main St. at Transit Rd
Williamsville
(716) 631-9730

Airport Plaza
4192 Union Road
Cheektowaga
(716) 634-1930

Southgate Plaza
1024 Union Road
West Seneca
(716) 675-4242

Mid City Plaza
1007 Payne Ave
North Tonawanda
(716) 694-7320

Mil Pine Plaza
8400 Niagara Falls Blvd
Niagara Falls
(716) 297-6161

5771 Camp Rd
Hamburg
(716) 648-1150

410 Kenmore Ave
Buffalo
(716) 832-5445

1205 Niagara Falls Blvd
Amherst
(716) 837-1900

ALBANY AREA

Travelers Building
80 Wolf Road, Colonie
(518) 454-3400

Downtown
126 State Street
(518) 434-6800

201 Broadway
Troy
(518) 271-8900

7 Clifton Country Rd
Clifton Park
(518) 371-1162

184 Delaware Ave
Delmar
(518) 439-2787

SYRACUSE/ UTICA AREA

One Park Place
300 South State Street
Downtown Syracuse
(315) 425-6800

212 Main Street
Oriskany Falls
(315) 821-7238

7505 Oswego Road
Liverpool
(315) 622-3301

162 Genesee Street
Downtown Utica
(315) 797-5500

6778 East Genesee St
Dewitt
(315) 445-0342

5852 East Circle Drive
Cicero
(315) 458-0013

5304 West Genesee St
Camillus
(315) 487-7100

204 Fayette Street
Manlius
(315) 682-8204

1 East Genesee Street
Skaneateles
(315) 685-8344

ROCHESTER AREA

155 East Main St
Downtown Rochester
(716) 546-0506

1 North Main St
Honeoye Falls
(716) 624-3800

Westmar Plaza
Buffalo and Pixley Rds
Gates
(716) 247-0180

Irondequoit
Plaza/Shopping Center
Hudson Ave. and Titus Ave
Irondequoit
(716) 544-0251

2655 E. Henrietta Rd
Henrietta
(716) 334-1682

625 Panorama Trail
Penfield
(716) 586-1872

3855 Dewey Ave
Greece
(716) 865-7430

2275 Ridge Road West
Greece
(716) 225-6594

3330 Monroe Ave
Pittsford
(716) 586-8953

Perinton Hills
Office Park
6707 Pittsford-Palmyra Rd
Fairport
(716) 223-5638

Culver Ridge Plaza
2255 Ridge Road E
(716) 342-6462

1441 Monroe Ave
Brighton
(716) 473-9080

Dewey Ridge
424 Ridge Rd. W
(716) 663-8211

24 Hr. Citicard
Banking Centers

Member F.D.I.C.
128602 11/1286

CITIBANK
Citibank (New York State), N.A.

CHECKING ACCOUNTS

Great choices, great value

CITIBANK
A CITICORP COMPANY

Select the plan that's right for you

When it comes to everyday banking needs, people aren't all alike. That's why Citibank offers three superior checking accounts. Each account can make checking simpler and more convenient. *All* of them offer these great benefits, and *one* of them is just right for you.

- **Unlimited Check Writing**—All three Citibank checking accounts offer unlimited check writing with no per check charges.
- **Comprehensive Statements**—Accurate, easy to read information is mailed to you each month to help you keep track of all your account transactions.
- **Citicard Cash Convenience**—You'll automatically receive a Citicard—your 24-hour cash connection—when you open any Citibank checking account. Citicard turns everyday banking into anytime, anyplace convenience.

Personal Checking

Personal checking is designed for those people who prefer to maintain a small balance in their checking account. The fees are low. In fact, there are absolutely no fees or charges if you elect to directly deposit your payroll or social security check into your account.

And all your checks are returned to you each month with a complete statement of all your transactions.

NOW Checking

Citibank's NOW account takes personal checking one step further by paying 5¼% interest on your entire checking balance. And when you keep an average balance of $1,000 in *any* combination of Citibank accounts, there are no monthly service charges.

Each month your checks are returned to you, along with a convenient statement that records all your account transactions—including the interest you've earned.

Citi-NOW

Citi-NOW offers high, money market rates on your checking balances with no monthly service fees.

By keeping $1,000 or more in your account you automatically earn money market rates, adjusted weekly for the highest possible interest on your checking dollars. And your account still earns interest—a full 5¼%—even if your balance falls below $1,000.

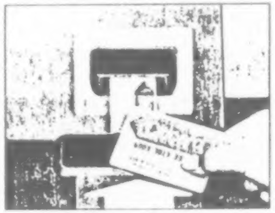
Your cancelled checks are conveniently stored at the bank,* and you receive a complete, easy-to-read monthly statement detailing your transactions and listing your checks in numerical order.

*Copies of specific checks are easily obtained, should the need arise.

You may never bounce a check again

Open any Citibank checking account and apply for Checking Plus* overdraft protection. It lets you write checks for more than your checking balance, and know they won't bounce. We'll automatically lend you what you need, up to your Checking Plus limit, to make sure your checks are covered.

Checking Plus costs you nothing until you use it, and you pay interest only on the amount you've borrowed. Checking Plus keeps you covered, just in case.



Citicard Banking makes your Checking even better

With Citicard, you have anytime, anyplace account access

You can check your balances and make deposits, withdrawals or transfers between linked accounts 24 hours a day at Citicard Banking Centers conveniently located at most Citibank branches throughout upstate New York and the New York metropolitan area.

Move your money where and when you want it

You can easily turn checking dollars into savings dollars that earn money market rates, or move savings dollars into checking so you can write checks when you need to. You can even make payments to other linked accounts like Ready Credit. All it takes is a simple transfer at any Citicard Banking Center. You'll get a record of all your Citicard transactions, and they'll also be listed for you on your monthly statement.

Added cash convenience

You can get cash at over 500 Metroteller® Automatic Teller Machines (ATM's) and other facilities located in supermarkets, drugstores, and gas stations throughout New York State. And if you're traveling out of state, Citicorp Cash^{SM} offers you access to over 5000 ATM's in a variety of electronic banking networks around the country.

Across the street, across the state, or across the country, you can get cash when and where you need it—instantly.

And getting the added cash convenience of Citicard is easy—all you have to do is ask! Any Customer Service Representative at a Citibank branch would be happy to help you.

	Regular Savings	**CASH MAXIMIZER**	**Personal Choice Time Deposits**
Minimum Opening Deposit	$100	$2 500	$2 500
Length of Term	NOT APPLICABLE	NOT APPLICABLE	7 days-10 yrs
Rate of Interest	Variable	Variable	Fixed
Security of FDIC Insurance up to $100 000	Yes	Yes	Yes
Additional Deposits Allowed	Yes	Yes	Yes during grace periods
Convenient Access via – Check – VERSATELLER ATM	 No Yes	 Yes Yes	 No No

CONVENIENCE SERVICES

– A support system for your savings and investments.

You want your banking to be as easy as possible so we provide support services that give you greater convenience and flexibility

VERSATELLER ATMs Over 1300 VERSATELLER ATMs make it easy for you to make deposits to, or withdrawals from, your Regular Savings and CASH MAXIMIZER account. You can also check your balance, as well as transfer funds between linked deposit accounts. Most VERSATELLER ATMs operate from 6 a.m. to midnight, 7 days a week, including holidays.

UNIFIED TIMESAVER STATEMENT.® If you have several accounts, you may benefit from a Unified TIMESAVER Statement at no extra charge. Information about your selected Regular Savings and Personal Choice Time Deposit accounts can be consolidated on your checking or CASH MAXIMIZER account statement. So you'll only have to look in one place for information about those accounts.

SAVINGS OVERDRAFT COVERAGE. This helpful service is security that we provide through Regular Savings to protect you from overdrawing your Bank of America checking account. When there are insufficient funds in checking, we'll automatically transfer money from your Regular Savings account to cover the amount of your check (minimum transfer $25).

COMBINED BALANCE SERVICE.® This is a great way to save money by avoiding monthly service charges on your checking account. All you have to do is keep a required combined balance in your Regular Savings account and in any one of your checking accounts.

If you'd like to know more about any of our services, a Customer Service Representative at any of our branches will be glad to help you.

FDIC INSURANCE— SECURE AND SOLID PROTECTION

Your funds on deposit with Bank of America are insured by the Federal Deposit Insurance Corporation (FDIC), an agency of the United States government. The total of all deposits held individually in your own name is insured up to $100 000. However, you can increase this coverage considerably by opening additional joint tenant and informal trustee accounts with other members of your family. This means that your insured amount can well exceed $100 000 and you can be secure in knowing that a greater amount of your hard earned funds are protected.

PLANS THAT GUARANTEE GROWTH

Whether you choose a savings and investment account that features convenience, flexible terms, or easy access, our range of plans all have one thing in common. They can make your money grow.

And no matter what kind of savings and investment program you need, at Bank of America we're always glad to sit down and help you choose the plan that's right for you. Just ask one of our Customer Service Representatives the next time you drop by. After all, you work hard for your money. Find out how hard we work to make it grow.

Information in this brochure is current as of July 1986 and is subject to change.

Bank of America
We want the job

Bank of America NT & SA - Member FDIC [illegible] Rev 7/86

Savings & Investments

Want to Make It Grow?

WASHINGTON
E DOL

SCHEDULE OF FEES PERSONAL ACCOUNTS

TRANSACTION ACCOUNTS

Personal Checking

Minimum balance $500 or more	No charge
Minimum balance less than $500	$5.00/month plus 20¢/check

NOW

Minimum balance $1,500 or more	No charge
Minimum balance less than $1,500	$5.00/month plus 20¢/check

Super NOW

All balances	0.02083% of average collected balance/month plus 10¢/check

All Transaction Accounts

Stop Payment	$20.00
Insufficient Funds Check	$20.00
Returned Deposited Check	$2.00
Certified Check	$10.00
Hold statements for customer pickup	$15.00/year
Personalized checks	dependent upon selection
Telephone balance inquiry	$1.00

SAVINGS ACCOUNTS

Maintenance Fee

Minimum balance $500 or more	No charge
Minimum balance less than $500	$2.00/month

Withdrawal Fees

Up to four per calendar quarter	No charge
More than four per calendar quarter	$2.00/ excess withdrawal
Hold statements for customer pickup	$15.00/year
Telephone balance inquiry	$1.00

MONEY MARKET ACCOUNT

Withdrawal fee	30¢/withdrawal or transfer
Insufficient Funds Check	$20.00
Telephone balance inquiry	$1.00

AUTOMATED TELLER MACHINE TRANSACTIONS

American Security Bank Machines	No Charge
Other Institutions Machines	
Through MOST* Network	$.55
Through Plus System, Inc.+	$1.00

BANKING CARDS

VISA Banking Card	$1.00/month
24-Hour Banking Card	No charge

WIRE TRANSFER

Domestic Incoming	
Credit to Account	$3.00
Mail Check to Valid Address	$10.00
Pay Check on Proper I.D.	$25.00
Domestic Outgoing	
Customer	$15.00
Non-Customer	$25.00
International Incoming	
Credit to Account	$10.00
Mail Check to Valid Address	$15.00
Pay Check on Proper I.D.	$25.00
International Outgoing	
Customer	$30.00
Non-Customer	$40.00
Other Services	
Telephone Advice of Incoming Wire	$3.00

SAFE DEPOSIT BOXES

1 x 5	$20.00/year
2 x 5	$25.00/year
3 x 5	$30.00/year
5 x 5	$50.00/year
3 x 10	$60.00/year
5 x 10	$100.00/year
10 x 10	$150.00/year
10 x 15	$225.00/year

The above listed sizes are the most common. All sizes may not be available at all branches.

Late payment fee	$5.00/month
Duplicate lost key	$5.00
Safe Deposit drilling	
Lost keys	$75.00
Non-payment of rent	$150.00

CHECKS/MONEY ORDERS

Cashier's Check	$4.00
Non-customer	$5.00
Money Order	$1.75
Travelers' Checks	1.0%
Stop Payment	
Money Order & Cashier's check	$20.00

GOVERNMENT BILLS/NOTES

If Purchased at auction	$45.00
If Purchased in open market	$55.00

---

* is a trademark of Internet, Inc

+ is a trademark of Plus System, Inc

MEMBER FDIC

courts and costs and expenses in connection therewith.

6. Interest will be paid in accordance with the option indicated from issue date at the interest rate set forth on the receipt for each Book Entry Time Deposit. Interest is calculated on the basis of 1/365 of a year's interest for each day (1/366 during leap year). Deposits of Public Bodies & deposits in amounts $100,000 or more are calculated on the basis of 1/360 of a year's interest for each day.

Individual Retirement Accounts

Individual Retirement Accounts give you the opportunity to build a more secure future for you and your family and possibly to save on income taxes now. Complete information is available at any First Interstate Bank branch on request.

Additional Rules Governing First Interstate Bank's Deposit Accounts

1. **Agreement.** You agree that your account will be governed by all the terms of this brochure, including the schedule of Account Service Fees and Rate Information, statements on the signature card, and applicable state and federal laws and regulations. We agree to be governed by them also.

2. **Deposits.** You may deposit cash or checks to your account. Deposits may be sent by mail or be made in person at any of our branches or Day & Night Teller facilities. We may at any time refuse a deposit or additional deposits.

3. **Collecting checks.** We have the right to obtain payment of checks and other items deposited by you before we make the money available to you to withdraw from your account. We collect a check you deposit by sending it for payment to the bank upon which it is drawn. Once the item has been finally paid, you may withdraw the money from your account. The Bank is authorized, without any responsibility on its part for loss in transit, to charge against the account any and all checks which may be deposited thereto or which may be cashed by us at your request and which we are unable to promptly collect. If we permit you to withdraw the money before the item has been finally paid and if it is not paid for whatever reason, we have the right to charge your account or obtain repayment from you for the amount of such item. All such returned checks may be mailed by unregistered mail to the last address shown on your Bank records.

4. **Statements.** Statements of your account will be sent to you by unregistered mail. For your protection and ours, notify us of any errors or improper charges to your account within 14 days after we mail or otherwise make the statement available to you. We will send the statement as well as any other communications to your current address appearing in our records for your account (if a joint account, to the address you select). Should a statement remain unclaimed or undeliverable for whatever cause, we may discontinue sending statements until we are instructed otherwise by you.

5. **Overdrafts.** If for some reason your account is overdrawn, you will receive notice but your statement normally will be held by us until the overdraft condition is corrected.

6. **Setoff.** The Bank retains a security interest in all accounts. If you owe us money and it is due, we have the right to use any or all of the money in this account or from any account you may have with us to pay the debt, regardless of the source of funds.

7. **Legal proceedings.** If your account becomes involved in legal proceedings, your use of it may be restricted. We shall be entitled to recognize any legal order or process served upon us which we reasonably believe to be binding, with no liability to you for doing so.

8. **Fees and service charges.** A schedule of our current service charge fees will be given to you when you open an account. You agree to pay the applicable charges promptly and authorize us to charge your accounts for these amounts. Charges may be changed from time to time by us with appropriate notice to you. See the Account Service Fees and Rate Information for current fees and service charges.

9. **Change of terms.** We shall not by reason of having waived in any instance any of the terms or provisions contained in these rules, be deemed thereby to have waived the same or similar or other terms or provisions in any other instances.

We may change the provisions, terms, and conditions of these rules at any time by sending a timely notice to you at the address shown on First Interstate's records for each account affected, prior to the date on which the change is effective. After such notice the amended or new rules shall be binding upon all depositors as though each depositor expressly assented to them, unless such change must be implemented immediately because of any law or regulation.

No sales charges!

America's High Yields from Scudder's Ginnie Mae Fund

High quality. High current yields. Looking for the high yields and high quality of Ginnie Maes, Fannie Maes, and Freddie Macs? Consider Scudder Government Mortgage Securities Fund. *Right now*, the Fund's investors are earning 8.5%.*

8.5%
7-day current yield

No sales charges. Unlike many Ginnie Mae funds, this Fund has no sales charges, no redemption or transaction fees, and no 12b-1 charges. And you benefit from free exchange among Scudder's 17 no-load funds.

Call or write today. We'll send you our free fact kit which explains more about the Fund's fluctuating yield and share price (for example, 5/19/86 and 5/19/87 share prices were $15.28 and $14.55).

SCUDDER GOVERNMENT MORTGAGE SECURITIES FUND
175 Federal St., Dept. 695, Boston, MA 02110

SCUDDER
800-453-3305
ext. 695

ontact Scudder Fund Distributors, Inc. for a prospectus containing more complete information including anagement fees and expenses. Read it carefully before you invest or send money. *8.5% is the Fund's t annualized yield for the 7 days ending 5/19/87. The value of your investment will fluctuate. If interest tes fall, share price will rise. If interest rates rise, share price will fall.

ALL-WEATHER STOCK FUND

T. ROWE PRICE EQUITY INCOME FUND. To weather all markets, this Fund follows a conservative strategy of investing in high-quality stocks that generate high income. It has delivered an impressive 54% total return since inception 10/31/85.* Past performance was achieved during a period of generally rising stock prices and is not indicative of future results. Minimum initial investment $1,000. *No sales charges.*

Mail coupon for a free information kit or call 1-800-443-8700, ext. 650

T. Rowe Price, 100 E. Pratt St., Baltimore, MD 21202
Send a prospectus with more complete information including management fees and other charges and expenses. I will read it carefully before I invest or send money.

Name

Address

City State Zip EFC650

Invest With Confidence
T.RowePrice

e Fund gained 54% since inception 10/31/85 to 4/30/87. Figures include changes in principal value, vested dividends and capital gains distributions—see page 14 of the Statement of Additional Informa- Market conditions fluctuated and past performance is not indicative of future results. T. Rowe Price stment Services, Inc., Distributor

---

MAIL THIS TO FIND OUT MORE ABOUT THREE OF THE BEST-PERFORMING FUNDS YOU'VE NEVER HEARD OF

You may not have heard of Criterion's three newest mutual funds, but Lipper Analytical Services has. Here are the funds' total returns for 1987 to date*

+55.9% Criterion Technology Fund
Ranked in top 2% of all 1,142 funds monitored by Lipper.

+33.8% Criterion Global Growth Fund
Ranked #3 of 37 funds in Lipper's Global category.

+13.6% Criterion Convertible Securities Fund
Ranked #2 of 346 funds in Lipper's Fixed-Income category.

*Change in net asset value plus reinvestment of all distributions 12/31/86 – 5/14/87. Does not include sales charges, which apply to most purchases. May differ from Lipper calculations. Past results do not guarantee future performance. Distributions and net asset value will fluctuate. Funds available only where registered.

Please send me prospectuses and more information, including management fees and expenses, on Criterion's new funds. I will read the material carefully before investing or sending money.

Name ____________________

Address ____________________

City, State, Zip ____________________

Day Phone ____________________

1-800-247-8236

CRITERION

1000 Louisiana, Houston, Texas 77002 070048

(7)

June 1987

Dear Customer:

On July 1, 1987, First of America will begin to pay interest on your account's "investable balance." All other features of the account will remain the same.

The investable balance recognizes the impact of federal reserve requirements. A federal reserve requirement is the portion of an account which a bank must hold in cash or in a non-interest-bearing account at the Federal Reserve Bank. Reserve requirement funds cannot be invested or loaned to people in the bank's community.

The accounts affected by this change are interest-bearing personal checking, business checking, and business savings. Personal savings accounts do not have a reserve requirement.

If you have any questions about this change, please contact your nearest branch.

Thank you for banking with First of America. We appreciate your business and invite you to consider us for all your financial needs.

FIRST OF AMERICA Bank

Members FDIC

"Hard Earned Cash" isn't just an expression. At Bank of America, we know how hard you work for your money, so we work hard to make your money grow. If you want a bank that helps you get the most out of your hard earned cash, ***we want the job.***

And that's why we offer such a wide range of savings and investment plans. With a choice of a Regular Savings account, the CASH MAXIMIZER® account, or our Personal Choice Time Deposits, you can be sure of flexibility, as well as the kind of terms which suit *you*. And with nearly 900 conveniently located B of A branches, and over 1300 VERSATELLER® Automated Teller Machines (ATMs), you'll quickly find out just how easy B of A banking can be!

REGULAR SAVINGS ACCOUNT

—A savings account for a solid start.

Your Regular Savings account is a good, solid foundation for a basic savings program. A low minimum deposit makes it an easy account to open, and with a VERSATEL® card your money is as easily accessible as your nearest VERSATELLER ATM.

That makes it the perfect account when you want to save for that sudden emergency, your dream vacation, or the new furniture you've had your eye on. And FDIC insurance means your money is protected. Your interest[*] compounds daily and is paid on the last day of every quarter.

Also, with our Savings Overdraft Coverage plan, a special feature of your Regular Savings account, you won't have to worry about overdrawing your checking account.

CASH MAXIMIZER ACCOUNT

—A maximum access investment account.

If you want an investment account with convenient checking privileges, that's exactly what your CASH MAXIMIZER account provides. You can write up to 3 checks[*] per statement period – an advantage that makes those unplanned purchases a lot easier to handle.

Your CASH MAXIMIZER account interest[**] is calculated daily and paid monthly on the last day of every statement period. Once you've made your opening deposit, you're guaranteed maximum convenience because you can make unlimited deposits and withdrawals by mail, by VERSATELLER ATM, or in person. FDIC insurance protects your investment.

PERSONAL CHOICE TIME DEPOSITS

—The tailor made account.

If you want a guaranteed rate, a Personal Choice Time Deposit is the investment for you. Leave your funds on deposit for a specified period of time and in return you get a guaranteed rate of interest.

A Personal Choice Time Deposit gives you great flexibility because, depending on the amount you choose to deposit, you can invest for as briefly as 7 days, or for as long as ten years – it's entirely up to you. And in many cases, you can even choose the exact maturity date!

You benefit from a fixed interest rate,[*] and can choose to have your interest paid monthly, quarterly, or annually. And for terms of one year or less, you can choose to have it paid at maturity. So you can have it when you need it most.

When your account matures, it can be automatically reinvested for another term. Or, you have the option, during a grace period, of adding to, withdrawing from, or changing the term of your account. And of course your funds are FDIC insured.

---

[*] Your rate of interest is variable and can change periodically, and may be higher depending on your balance. If your account is closed before the end of the quarter, interest for that quarter will not be paid.

[*] You can make up to 6 third party transfers per statement period, 3 of which can be by check and/or VERSATEL Payment Service.

[**] Your rate of interest is variable and can change periodically, and may be higher depending on your balance. If your account is closed before the end of the statement period, interest for that period will not be paid.

[*] Substantial interest penalty for early withdrawal.

INVESTMENT SERVICES FOR AMERICA

INVEST™

- Stocks
- Bonds
- Retirement Accounts
- Mutual Funds
- Tax-Advantaged Investments
- Portfolio Management Services
- Financial Planning

See the INVEST Representative at the locations listed below:

Downtown 879-7175
1700 Pennsylvania Avenue, N.W.

Chevy Chase 879-7226
5301 Wisconsin Avenue, N.W.

Springfield, VA 879-7599
8440 Old Keene Mill Road

Bethesda, MD	**879-7256**
4825 Cordell Avenue	**879-7300**

A SERVICE OF ISFA CORPORATION   MEMBER SIPC

Columbia First
Federal Savings & Loan Association

Administrative Office
*610 13th Street, N.W.
Washington, D.C. 20005
Telephone (202) 879-7100
**Monday-Friday 9 a.m.-4 p.m.

District of Columbia Locations

*730 11th Street, N.W.	879-7120
*1101 15th Street, N.W.	879-7130
*2000 L Street, N.W.	879-7140
*1800 M Street, N.W.	879-7150
1200 New Hampshire Avenue, N.W.	879-7160
1700 Pennsylvania Avenue, N.W.	879-7170
*1900 Pennsylvania Avenue, N.W.	879-7180
4857 Massachusetts Avenue, N.W. Friday 9 a.m.-6 p.m.	879-7190
4340 Connecticut Avenue, N.W. Friday 9 a.m.-6 p.m.	879-7200
*5005 New Hampshire Avenue, N.W. Saturday 9 a.m.-noon	879-7210
*5301 Wisconsin Avenue, N.W. Friday 9 a.m.-6 p.m.	879-7220
*3216 Pennsylvania Avenue, S.E.	879-7230
300 7th Street, S.W.	879-7240

Maryland Location

*4825 Cordell Avenue, Bethesda, Md. Lobby: Monday-Friday 9 a.m.-3:30 p.m. Saturday 9 a.m.-noon Drive-In: Monday-Friday 8 a.m.-6 p.m. Saturday 9 a.m.-noon	879-7250

Virginia Locations
Lobby hours are 9 a.m.-noon each Saturday

6926 Braddock Road, Annandale	879-7575
9400 Burke Lake Road, Burke Drive-In: Monday-Friday 9 a.m.-7 p.m. Saturday 9 a.m.-2 p.m.	879-7580
3095 Nutley Street, Fairfax Drive-In: Monday-Friday 9 a.m.-7 p.m. Saturday 9 a.m.-2 p.m.	879-7585
1601 Washington Plaza, Reston Walk-Up: Monday-Friday 8-9 a.m. & 4-7 p.m. Saturday noon-2 p.m.	879-7590
8440 Old Keene Mill Rd., Springfield Drive-In: Monday-Friday 9 a.m.-7 p.m. Saturday 9 a.m.-2 p.m.	879-7595

Virginia Loan Office

3091 Nutley Street, Fairfax	879-7588

Home Service Insurance Agency
A WHOLLY OWNED SUBSIDIARY OF COLUMBIA FIRST

610 13th Street, N.W.	638-1776
2000 L Street, N.W.	955-5873
5005 New Hampshire Avenue, N.W.	829-3752
3091 Nutley Street, Fairfax, VA	879-7589
4825 Cordell Avenue, Bethesda, MD	879-7257/652-5270

INVEST Centers
AN INDEPENDENT SERVICE OF ISFA CORPORATION MEMBER SIPC

1700 Pennsylvania Avenue, N.W.	879-7175
5301 Wisconsin Avenue, N.W.	879-7226
8440 Old Keene Mill Road, Springfield, VA	879-7599
4825 Cordell Avenue, Bethesda, MD	879-7256/879-7300

*MOST Automated Teller Machine Available
**Lobby hours are Monday-Friday 9 a.m.-4 p.m. except where noted.

Savings and Investments: Rate Chart

Columbia First
Federal Savings & Loan Association

They don't call us first for nothing.

Savings and Investments

RATES EFFECTIVE MARCH 11, 1987
Interest rates subject to change on a daily basis. For current information please call our 24-Hour Rate Line, 879-7260.

TYPE OF ACCOUNT	MINIMUM TERM	MINIMUM DEPOSIT	INTEREST RATE	ANNUAL YIELD	EARLY WITHDRAWAL FORFEITURE
REGULAR	NONE	$50	5.50%	5.73%	NONE
NOW SUPER NOW	NONE NONE	$200/500 $2500	5.25% 5.65%	5.47% 5.90%	NONE NONE
MONEY MARKET	NONE	$2500	5.80%	6.06%	NONE
CERTIFICATE	3 MONTHS	$500	5.85%	6.11%	1 MONTHS INTEREST
CERTIFICATE	6 MONTHS	$500	6.00%	6.27%	1 MONTHS INTEREST
CERTIFICATE	12 MONTHS	$500	6.30%	6.60%	1 MONTHS INTEREST
CERTIFICATE	24 MONTHS	$500	6.60%	6.92%	3 MONTHS INTEREST
CERTIFICATE	36 MONTHS	$500	6.80%	7.14%	4 MONTHS INTEREST
CERTIFICATE	48 MONTHS	$500	7.00%	7.35%	4 MONTHS INTEREST
CERTIFICATE	60 MONTHS	$500	7.10%	7.46%	6 MONTHS INTEREST
NEGOTIABLE CERTIFICATE	3,6,9,12 MONTHS	$ 50,000	CALL 879-7100	SIMPLE	1 MONTHS INTEREST
NEGOTIABLE CERTIFICATE	NEGOTIABLE	$100,000	CALL 879-7100	SIMPLE	1-6 MONTHS INTEREST

OTHER INFORMATION

INTEREST ON ALL NON-NEGOTIABLE ACCOUNTS, IS COMPOUNDED DAILY

EARLY WITHDRAWAL FORFEITURE
Except as otherwise provided in the account agreement, in the event of any withdrawal of principal prior to a maturity date, the accountholder shall forfeit an amount equal to interest for the period specified in the account agreement, whether earned or not, on the amount withdrawn at the nominal rate paid on the account regardless of the length of time the funds withdrawn have remained in the account.

NOW/SUPER NOW
If balance drops below $2,500 during cycle, interest 5.25%. $500 minimum balance requirement during cycle if checks returned or $5 monthly service charge. $200 minimum balance requirement during cycle if checks not returned or $4 monthly service charge.

MONEY MARKET DEPOSIT ACCOUNT
If balance drops below $2,500 during month, maximum interest 5.25%. $5 monthly service charge on balance of less than $500. Accountholder may issue up to 3 checks and 3 pre-authorized or automatic transfers each month.

ACCOUNT STATEMENTS
Monthly statements are issued for N.O.W., Money Market and Statement Savings accounts. Certificates not receiving interest checks are issued statements quarterly.

Senator Dodd. Mr. Shipman, we welcome you.

STATEMENT OF JACK SHIPMAN, EXECUTIVE VICE PRESIDENT, LIBERTY NATIONAL BANK AND TRUST CO., LOUISVILLE, KY, REPRESENTING THE AMERICAN BANKERS ASSOCIATION

Mr. Shipman. Mr. Chairman and members of the subcommittee, I am Jack Shipman, executive vice president, and it's Liberty National Bank which was omitted and it's not just the National Bank in the submitted testimony, in Louisville, KY, a member of the Branch Administration Committee of the American Bankers Association.

The American Bankers Association is a professional and trade association for the commercial banking industry. The combined assets of our members represents approximately 95 percent of the total industry.

We welcome the opportunity to present the Association's views on S. 1507, the Truth in Savings Act.

The American Bankers Association supports the intent of S. 1507 insofar as it assures the availability of simple and understandable information which provides the public the opportunity to make intelligent shopping comparisons.

MAJOR SEGMENTS OF S. 1507 QUESTIONED

However, our overriding concern is that major segments of the public will not be protected by S. 1507 because it does not extend coverage to nondepository competitors such as mutual funds and others who offer competitive instruments.

In many respects the legislation currently before the subcommittee reflects the widespread disclosure practices already underway in our industry to ensure that consumers are able to make educated decisions on where they place their money. We have conducted surveys and, contrary to some of the statements made, I don't believe that there is very widespread misuse of this advertising.

We have urged our members to take voluntary action on full disclosure of rates on deposit accounts and have assisted them by preparing a banker action kit to help individual banks formulate a rate disclosure advertising plan for their own institutions.

In light of our concern for a full disclosure concerning depository accounts, our Association supports the thrust of this legislation as being an appropriate accompaniment to those voluntary efforts.

Unfortunately, however, S. 1507 does not take into account the vast changes in saving markets which have occurred in recent years. Improvements in technology and the restrictions on interest rates help contribute to the spectacular growth of money market funds as an available and attractive alternative to traditional banking savings accounts.

Moreover, the recent bull market has increased the popularity of mutual funds. With the elimination of government imposed ceilings on rates paid on savings accounts a variety of competing market rate savings instruments have been created which provide the benefits of higher yields to many savers.

These new choices afford savers and financial institutions the opportunity to select options best suited to their particular interests, but the resulting array of competitive advertising makes clear and uniform disclosure of terms vital to consumer understanding. It also underscores the necessity of including both nondepository as well as depository institutions under any advertising disclosure legislation regulations to help the consumer make informed decisions about his savings dollar.

Arguments can be made that mutual funds and savings deposits are legally distinct products. There is no doubt that an investment in a mutual fund results in an ownership relationship, whereas a deposit in a savings account results in a creditor relationship.

However, from the viewpoint of the consumer, which is what I think we're talking about today, both mutual funds and savings accounts are viewed as functionally the same. They offer an opportunity to obtain a return on that consumer's savings dollar. Therefore, adequate disclosure must be made by both banks and mutual funds so that that consumer can evaluate and compare the risk and the benefits that he's about to receive.

COMPETITION FOR SAVINGS

Mutual funds, securities firms and others who offer competitive instruments have become an active competitor with banks for the consumer's savings dollar. A good example of this is the competition of mutual funds for consumer savings.

A mutual fund is a diversified portfolio of securities under professional management and common ownership. Increasingly mutual funds are being tailored to meet specialized consumer needs. Investment companies have developed extensive families of mutual funds to meet a wide range of investment objectives. Today there are mutual funds designed to satisfy just about every investor's needs.

Consumers' response to mutual funds opportunities have been remarkable. A few statistics, if you will——

[A note was handed to Mr. Shipman.]

Mr. **SHIPMAN**. Let me give the statistics. I think that's probably very important.

Senator **DODD**. I just noticed you were on page 4 of a 14 page statement.

Mr. **SHIPMAN**. Oh, I've got more pages, but they are not going to be testified on.

Senator **DODD**. I just got worried, that's all. [Laughter.] Office of the Secretary.

Mr. **SHIPMAN**. I guess that's Kentucky——

Senator **DODD**. I know Kentucky very well. [Laughter.]

Mr. **SHIPMAN**. But a few statistics on the subject of what we're talking about. The investment company institute estimates that there were 35 million mutual fund accounts in 1985, which represent ownership by 22 million households. Assets of stock funds and income funds have jumped from $58.5 billion in 1980 to $424.2 billion by 1986, which represents an increase of over 600 percent.

According to a recent Business Week article, mutual fund companies had total assets of $716 billion at the end of last year, and by the end of 1987 it will be a $1 trillion industry.

I appreciate the opportunity to testify today.

Senator **Dodd**. Well, Mr. Shipman, I appreciate that as well and, as I said, your full statement will be made part of the record. I have some questions for you which may bring out an awful lot of what else was in the testimony.

[The complete prepared statement of Jack Shipman follows:]

CFA
Consumer Federation of America

June 3, 1987

Hon. Robert L. Clarke
Comptroller of the Currency
490 L'Enfant Plaza East, SW
Washington, DC 20219

Dear Mr. Clarke:

In the course of conducting Consumer Federation of America's fourth annual survey of bank fees, we have encountered a practice used by several federally-chartered commercial banks to overstate the rate of interest they pay consumers for their deposits.

The practice is described by most of these banks as paying interest on the consumer's "investable balance." The material we have received from these banks indicates that they calculate the balance on which interest is paid by reducing the collected or ledger balance by a percentage equal to the bank's reserve requirements.

We believe this practice is unfair and deceptive and that it is described to consumers in terms that incorrectly imply a legal requirement that interest be paid in that manner. On behalf of CFA, I ask that you inform the banks under your jurisdiction that this practice is unlawful unless the appropriate interest rate and yield are adjusted to reflect the effects of the technique.

We have enclosed copies of disclosure materials from six banks that appear to use this technique. I have spoken with employees of all six banks, and have confirmed that four actually apply this technique to at least some of their consumer accounts. A fifth bank uses the technique on its commercial accounts and has reserved the right to extend this practice to its consumer accounts, but has not yet done so. Employees at the sixth bank were unable to tell us whether the investable balance method is currently in use.

According to these materials and our conversations with bank personnel, the following are the policies maintained by these banks:

*Bank IV, Kansas, pays 4.75% interest on 88% of the customer's balance in a Money Market Checking Account.

1424 16th Street, N.W., Suite 604 • Washington, D.C. 20036 • (202) 387-6121

*Union National Bank & Trust, Kansas, uses this method on its Interest on Checking and Super NOW accounts. Account balances are reduced by "about 3%," we were told.

*RepublicBank South Austin, Texas, uses the technique on several of its accounts. The current deduction is about 6% of the balance. We believe, from the information provided by that bank, that the technique is used by all banks in the RepublicBank holding company; that the proportion by which balances are reduced varies from subsidiary to subsidiary depending on the reserve requirements of each bank; and that the proportion may be adjusted periodically to reflect current reserve requirements.

*American Security Bank, Washington, DC, pays 5.30% interest (5.25% on balances under $2500) on 88% of the balance in a Super NOW account.

*National City Bank, Ohio, pays interest on 88% of the balance in commercial accounts. The bank's consumer account contract allows the bank to pay interest on the basis of the investable balance, but we were told the practice has not been initiated.

*Signet Bank, Maryland (formerly Union Trust Bank) has one brochrue, dated February 11, 1987, that allows the use of this method. We were not able to determine whether the bank has used this method in the months since its acquisition by Signet was completed.

A bank that pays 4.75% interest on 88% of a consumer's balance should have no right to use the 4.75% figure. That bank is really paying 4.18%, and should not be allowed to claim anything more.

We ask you to tell banks under your jurisdiction that interest must be calculated on the basis of the full balance in an account, and that any exclusion from the full balance must result in a proportionate adjustment of the disclosed interest rate and yield. If banks can unilaterally decide to pay interest on any portion of the balance they desire, then the annual rate of simple interest will have no meaning and consumers will be unable to determine which bank pays which rate of interest.

We urge you to act expeditiously to protect consumers from this unfair and deceptive practice.

Sincerely,

Alan Fox

Alan Fox
Legislative Representative

Enclosures

Comptroller of the Currency
Administrator of National Banks

Washington D C 20219

July 24, 1987

Mr. Alan Fox
Legislative Representative
Consumer Federation of America
1424 16th Street, N.W., Suite 604
Washington, D.C. 20036

Dear Mr. Fox:

This is in reply to your June 3, 1987 correspondence in which you expressed concern with an interest-payment practice of certain federally-chartered commercial banks. The material that you provided indicates that some banks calculate interest on deposit balances by reducing the collected ledger balance by a percentage equal to that which the bank is required to maintain with the Federal Reserve Bank. This practice, which you have characterized as unfair and deceptive, is generally described as payment of interest on the consumer's "investable" balance.

You have asked us to require banks under our jurisdiction to calculate interest on the basis of the full balance in the account and that any exclusion from the full balance must result in a proportionate adjustment of the disclosed interest rate and yield.

We do not believe that paying interest only on the "investable" balance, as defined by these banks, is by itself unlawful. The practice of paying interest on the portion available to invest reflects one way that a bank uses to price its accounts. However, advertisements of banks that price their accounts in such a manner must include reference to that practice.

We have reviewed the bank disclosures that you provided and we share some of your concerns about the accuracy of these disclosures. If a bank computes interest on deposit balances that are less than collected amounts, the bank should clearly disclose that fact to the depositor or, alternatively, reduce any advertised interest rate or yield by an amount to account for the difference. Also, if an advertisement or disclosure states or implies that Federal Reserve requirements prohibit the payment of interest on a portion of the consumer's deposit, such an advertisement would be misleading, inaccurate and a violation of Regulation Q (12 CFR 217.6(g)).

As we identify bank problems, whether during examinations or by any other means, documentation of the problem is furnished to the appropriate District or Field Office for review and follow-up. With respect to the information that you provided us, we will be taking the necessary steps to ensure that the affected institutions advertise the nature of their deposit accounts properly.

Besides requiring compliance with specific legal requirements, OCC has consistently urged national banks to disclose fully to the consumer, when an account is opened, the methods they use to compute the balance on which interest is paid. We are currently working with other federal regulators of depository institutions and the Federal Financial Institutions Examination Council on related issues.

To focus attention on these issues further, we are sending an Advisory Letter to all national banks. The advisory will focus specifically on the bank practice of paying interest on only a portion of the depositor's account balance.

We remain committed to ensuring that bank disclosures and advertisements are accurate, representative of deposit contracts and not misleading. We continue to require banks that act contrary to these principles to correct their practices. We appreciate your having brought this matter to our attention.

Sincerely,

Robert L. Clarke
Comptroller of the Currency

Statement of the
American Bankers Association
on the
Truth-in-Savings Act, S.1507
Presented to the
Subcommittee on Consumer Affairs
Committee on Banking, Housing and Urban Affairs
United States Senate

August 5, 1987

Mr. Chairman and members of the Subcommittee, I am Jack Shipman, Executive Vice President of the National Bank and Trust Company in Louisville, Kentucky. I am also a member of the Branch Administration Executive Committee of the American Bankers Association.

The American Bankers Association is the professional and trade association for the commercial banking industry. The combined assets of our members represent approximately 95 percent of the industry total. We welcome the opportunity to present the Association's views on S.1507, the Truth in Savings Act.

The American Bankers Association supports the intent of S.1507 insofar as it assures availability of simple and understandable information which provides the public the opportunity to make intelligent shopping comparisons. However, our overriding concern is that major segments of the public would not be protected by S.1507 because it does not extend coverage to nondepository competitors such as mutual funds and others who offer competitive instruments.

In many respects, the legislation currently before the Subcommittee reflects the widespread disclosure practices already underway in our industry to ensure that consumers are able to make educated decisions on where they place their money.

We have urged our members to take voluntary action on full disclosure of rates on deposit accounts and will continue to do so. As part of this effort, the ABA has prepared a banker-action kit to help individual banks formulate a plan for their own institutions. The kit (attached to this statement) contains guidelines for rate-disclosure advertising that are very similar to the provisions found in this bill. The guidelines in our packet also include samples of "right" and "wrong" advertisements and explanations of each.

In light of our concern for full disclosure concerning depository accounts, our Association supports the thrust of this legislation as being an appropriate accompaniment to these voluntary efforts. Yet, this legislative endeavor has a shortcoming which we hope will be dealt with as the Subcommittee proceeds with mark-up of the bill.

S.1507 does not take into account the vast changes in savings markets which have occurred in recent years. Improvements in technology and the restrictions on interest rates helped contribute to the spectacular growth of money market funds as an available and attractive alternative to traditional bank savings accounts. Moreover, the recent bull market has increased the popularity of mutual funds. With the elimination of government-imposed ceilings on rates paid on savings counts, a variety of competing market-rate savings instrume s have been created which provide the benefits of higher lds to many savers. These new choices afford savers and fin ial institutions the opportunity to select options best su d to their particular interests. But, the resulting array o ompetitive advertising makes clear and uniform disclos of terms vital to consumer understanding and undersc s the necessity of including both nondepository as well as pository institutions under any advertising/ disclos legislation.

Ar ents can be made that mutual funds and savings deposit re legally distinct products. There is no doubt that an inve ent in a mutual fund results in an ownership relatio ip whereas a deposit in a savings account results in a credito elationship. However, our focus must be on how the consume iews these products. From the viewpoint of the consume both mutual funds and savings accounts are viewed as functio lly similar: they offer an opportunity to obtain a return savings dollars. Therefore, adequate disclosure must be made both banks and mutual funds so that the consumer can evalua and compare the risks and benefits.

M al funds, securities firms, and others who offer compet ve instruments have become active competitors with banks the consumer's savings dollar. A vivid example of this he competition of mutual funds for consumer saving

A mutual fund is a diversified portfolio of securities under professional management and common ownership. Increasingly, mutual funds are being tailored to meet specialized consumer needs. Investment companies have developed extensive "families" of mutual funds to meet a wide range of investment objectives. Today, there are mutual funds designed to satisfy just about every investor's needs. A potential investor can put money in mutual funds in international stocks, stock indices, convertible bonds, precious metals, junk bonds, government bonds and Ginnie Mae mortgage-backed securities, as well as money market funds.

Consumers' response to mutual fund opportunities has been remarkable. A few statistics on the subject illustrate that. The Investment Company Institute estimates that there were 35 million mutual fund accounts in 1985, representing ownership by 22 million households. Assets of stock, bond and income funds have jumped from $58.4 billion in 1980 to $424.2 billion by 1986 -- an increase of over 625 percent in just six years. According to Business Week, mutual fund companies had total assets of $716 billion at year end, and by the end of 1987 it will be a $1 trillion industry.

Total sales of stock, bond and income funds in 1986 reached a record $215.7 billion, almost double the previous record of $114 billion set in 1985. New sales (sales less reinvested dividends) amounts to over $550 million per day during 1986. Sales of bonds and income funds exceeded equity fund sales by a three to one margin during 1986; the biggest increase in the bond and income category were government income funds and Ginnie Mae funds.

Along with their growing attractiveness, mutual funds, particularly bond funds, have become the subject of increasing criticism over advertising abuses. The funds have been attracting potential customers with eye-catching descriptions of substantial yields. What the advertisements fail to indicate in many cases, however, is that the yield mentioned may actually reflect the fund's performance several months ago.

Because it is impossible to predict accurately future market fluctuations, bond and other income funds do not provide figures on what future yields might be. Instead, they have used, on a selective basis, previous figures which have been particularly attractive. Since there have not been clear guidelines established as to what periods of time they should be using for those advertisements, some funds may utilize rather stale figures simply because they represent periods of particularly high yields.

Often consumers do not realize that while the advertised yield on a bond or certificate of deposit represents a legally enforceable rate of return, the advertised yield of a mutual fund actually represents no more than the historical rate the fund has been able to achieve in the past. It is no guarantee of future earnings.

Mutual funds have not adequately disclosed in their advertising, the historical nature of the data presented or the risks that principal as well as income may fluctuate due to market conditions. It may therefore come as a surprise to potential bond fund customers, that there is the possibility of a financial loss of principal in some circumstances. In funds where bonds are held to maturity, market fluctuations may not ultimately effect the investor because the bond may be held to maturity. But in Ginnie Mae funds, the underlying mortgage, if prepaid, may result in a loss. For example, if the mutual fund has purchased securities backed by mortgages with a high interest rate and paid a premium and then the homeowners whose mortgages underly the certificates refinance their mortgage when mortgage rates drop, doing so at par, the fund (and as a consequence the fund's shareholders) may actually suffer a loss.

Furthermore, a potential mutual fund customer is unlikely to realize that the "yield" displayed in advertisements means different things even among different mutual funds. There is no uniform method of yield computation. Hence, comparison shopping among mutual funds has been extremely difficult if not impossible.

A study conducted by Forbes Magazine last March revealed that of the 12 funds surveyed, only one defined yield the way the average investor would: current income once deductions have been made for expenses, divided by the net asset value per share. Instead "yield" varied widely, with one firm using anticipated dividends and gains, while another chose to

Senator Dodd. Mr. Silver.

STATEMENT OF DAVID SILVER, PRESIDENT, INVESTMENT COMPANY INSTITUTE

Mr. Silver. Thank you, Mr. Chairman.

First, I would like to thank Mr. Shipman for the plug for mutual funds. I hope we make the trillion dollar mark.

I am David Silver, president of the Investment Company Institute and the National Association of the American Mutual Fund Industry.

Mutual funds are subject to stringent disclosure and advertising regulations administered by the Securities and Exchange Commission. We wholeheartedly support S. 1507 which would improve the quality of information available to the investing public about other financial products.

Further, we believe that the bill can be improved to provide a broad framework in which to harmonize the regulation of advertising of bank product with the regulation of SEC registered product, most notably mutual funds.

PROPOSED AMENDMENTS TO S. 1507

We therefore would propose two amendments to perfect this already excellent bill.

Mutual funds have long been subject to a comprehensive system of regulation under the Federal Securities Law. Shares of mutual funds are continuously registered under the Securities Act of 1933 and therefore are subject to the act's disclosure and updating requirements on a continuing basis.

There are three types of disclosure documents permitted to mutual funds under the Securities Act, the prospectus, a comprehensive disclosure statement that must be provided to all investors; second limited kinds of advertising which solicit investors to request copies of the prospectus and, finally, sales literature which may supplement but not replace the statutory prospectus.

The SEC has adopted specific rules for mutual funds in all three areas of communication and continuously responds to new products and investor needs with new rules and rule amendments.

EXAMPLE OF SEC RULE AMENDMENTS

For example, in 1980 the SEC adopted rule amendments establishing a single uniform formula for advertising yields of money market funds, the mutual fund product which competes most directly with bank deposits.

Recently there has been a sharp increase in consumer interest in mutual funds investing in bonds and other long-term debt instruments. After suggestions of a special industry committee were formulated in March 1986, the SEC in September proposed extensive new rules to govern advertising by all income funds.

Although the industry and the SEC staff are in disagreement over portions of the proposed rules, the SEC proposal does include a standard yield calculation formula for income funds that is substantially the same as the formula suggested by the industry.

calculate it by taking the last 12 months of interest which was higher than the current rate and then boosting it further by adding capital gains. Yet another took interest for a seven day period and capital gains for the quarter and then projected them for a year. In short, a wide range of computations was used to produce a "yield" that would attract the consumer.

Mutual funds have also been guilty of other advertising abuses as well. Often advertisements will not indicate that there are expenses which may be incurred in owning a particular mutual fund. For instance, advertisements may not disclose that there are front loads (sales charges) or commissions or that the mutual fund has a 12b-1 plan -- a plan in which the fund management is permitted to deduct some money from the mutual fund assets each year to defray distribution costs including sales or marketing, advertising, and printing. All of these decrease customer earnings and if disclosed in the advertisement might determine which fund a consumer purchases.

One type of fund in which there has been a substantial amount of misleading advertisement are the Ginnie Maes. Ginnie Maes are mortgage backed securities created about 25 years ago to help moderate income consumers purchase homes. Originally only purchased by wealthy individuals or institutions, these securities are now available to average persons through mutual funds which purchase them in large denominations and sell shares in the funds in more affordable denominations. These funds

account for approximately $18 billion dollars in investments. Furthermore, they are a prime example of why nondepository institutions should be regulated by S.1507.

The unwary reader of many Ginnie Mae fund advertisements is not told that U.S. government guarantees relate only to timely payments on the underlying mortgage-backed securities. There is no federal guarantee of the mutual funds' dividends, solvency, capital appreciation, current return or yield.

With all these pitfalls in the marketplace and no consistency in advertisements, it is no wonder that consumers are confused about investment options. According to a survey conducted by Market Facts, Inc., a Chicago research group, of the 1,600 households questioned, only one-fourth of all mutual fund investors felt they understood how their mutual funds operated. Yet, the bill being considered would not require mutual funds and others who offer competitive instruments to adhere to similar advertising rules as those proposed for banks.

As competition for the consumer dollar increases, it is likely that there will be a greater flood of ads trying to attract consumers with exaggerated promises of high yields and terrific deals. Deceptive or inconsistent advertising practices make it important for Truth-in-Savings legislation to include the regulation of mutual funds and other nondepository institutions as part of the law. If a consumer is to be assured of having access to comprehensive information for comparison shopping before deciding, then disclosure requirements must be required of all possible sources for savings, not just depository institutions.

During this hearing, our members also want to point out that they support the reasonable disclosure of pertinent features of depository accounts as long as any new disclosures are meaningful, easily understood and useful for purposes of choosing an account.

However, it is just as important to make a distinction on the one hand, between providing sufficient information in advertisements, schedules, and other materials for a potential customer to make a choice and, on the other hand, numbing the customer's comprehension with an excess of them. When disclosures become too-lengthy or difficult to understand, consumers ignore them. This ultimately defeats the purpose of providing them. With this in mind, we would like to make some other recommendations regarding S.1507 to help streamline the legislation and improve consumer information.

THE ELECTRONIC MEDIA

Subsection 3(b) permits the Board, by regulation, to exempt electronic media advertisements from a few disclosure requirements if "any such disclosure would be unnecessarily burdensome." Those disclosure exemptions include: the minimum amount of initial deposit required to open the account in order to obtain the yield advertised if it is greater than the minimum balance necessary to earn that yield; the annual rate of simple interest and a statement that regular fees or other conditions

could reduce the yield if applicable. But in reality, any disclosure requirement for radio and television advertisements would be burdensome. Congress, therefore, should exempt all of them from the disclosure requirements.

Electronic media advertisements tend to run a mere 15, 30 or 60 seconds in length. Despite this, S.1507 would require that those advertisements include a number of lengthy disclosures within a very limited time frame. Not only will this confuse viewers and listeners, but it will also detract from the advertisement's marketing value. Moreover, since the complete features of the account are eventually disclosed in full before the consumer makes a commitment, such disclosure requirements for electronic media advertisements are unnecessarily burdensome.

MISLEADING DESCRIPTION OF FREE OR NO-COST ACCOUNTS PROHIBITED

Our Association members also believe that Subsection (3)(c) dealing with misleading descriptions of free or no costs accounts should be eliminated from the legislation. Although this is clearly a well intentioned provision, it would have the unfortunate effect of discouraging banks from designing products to benefit market segments which have difficulty using banking services today.

This subsection is unnecessarily restrictive and will inhibit the development of basic banking programs designed to benefit the elderly and poor.

SCHEDULE OF FEES

Subsection 4(d) requires that schedules include additional disclosures if the Board determines such information assists the customer in understanding and comparing accounts. To avoid confusion, we believe the provision should clarify that depository institutions need not disclose nonrecurring charges imposed for nonregular and extraordinary services, such as charges for travelers checks, wire transfers, and check printing. The price of these separate services does not generally influence the choice of a deposit account. When signing up for a deposit account, a prospective customer is likely to review with care the specifics of a deposit account. That same consumer is far less likely to be concerned with a single event, such as a wire transfer or the purchase of occasional travelers checks. The addition to the schedules of such information could be costly for institutions and would lengthen disclosures, thus diluting their impact.

CALCULATION ON FULL AMOUNT OF PRINCIPAL

We also advocate some revisions of Subsection 7(a) which requires that the amount of interest accruing on an interest-bearing account be calculated by utilizing the full balance for computation purposes. This section's objective is to require disclosure when a bank is using an investable balance method of computation. We support disclosure of this fact. However, the wording of this amendment has resulted in considerable confusion leading many to conclude that it is intended to

prohibit investable balance products rather than require clear disclosure. Therefore, we suggest that the sentence be re-written as follows:

> "If the annual percentage yield is calculated on less than the full amount of principal in the account, then the depository institution shall be required to disclose what the annual percentage yield would be, if calculated on the full amount of principal in the account for the stated calculations period at the rate or rates of interest disclosed pursuant to this Act."

This would enable Congress to achieve its goal of full disclosure of the investable balance method of computation while eliminating any confusion which the Board may encounter in attempting to translate the legislative mandate into regulations.

To further assist the public and the regulators, we suggest that the disclosure requirement be moved from Subsection 7(a) to Subsection 3(a) and be included in the list of disclosures described therein.

Moreover, Subsection 7(b) which indicates that no particular method of computation of interest is required, would be more appropriately placed as Subsection 3(e).

STATE LAW

The objective of this legislation is to provide for uniform disclosures which will enable consumers to comparison shop for investments more effectively. With the increasing number of bank mergers and acquisitions, achieving such consistency in disclosure will be unattainable if state laws are allowed to supercede federal law, as has been proposed in Section 12. Congress is best equipped to craft legislation on Truth-in-Savings to cover all states activities. To permit state law to supercede federal law would obviate the goals of this legislation and cause consumers unnecessary confusion as to whether the information they have received from Bank A is really comparable to that received from Bank B. We would therefore urge that Section 12 be amended to reflect federal precedence in Truth-in-Savings laws.

CONCLUSION

The American Bankers Association wishes to underscore its commitment to providing consumers with clear and comprehensive information so that they may make educated decisions on which deposit accounts meet their needs. We believe, however, that in order to achieve this goal, mutual funds and others who offer competitive instruments must be included in S.1507 and some additional modifications (which we have outlined) must also be implemented.

We wish to thank the Subcommittee for letting us present the views of the Association on this proposed legislation and again stress that we will continue to work with the Congress to improve consumer information on deposit accounts.

ATTACHMENT 1

RATE DISCLOSURE:
GUIDELINES FOR ADVERTISING

In general, for any advertisement, announcement or solicitation of savings and deposit instruments, depository institutions should explain the terms and conditions of the account in simple direct language. A depositor should be able to understand easily the relative merits of competing offers and intelligently choose those that best suit his or her needs. Any solicitation which states the interest rate paid should clearly disclose the annual rate of interest, the annual percentage yield and the method by which interest on the account is compounded.

Specifically, to give consumers information with which to make meaningful comparisons, advertisements regarding the rate of interest should include the following:

- o Annual percentage yield and the method of compounding.
- o Annual rate of simple interest and the length of time the rate is effective.
- o The frequency with which interest is payable.
- o Minimum balance requirements.
- o Clear disclosure of penalties for early withdrawal and any fees.
- o Annual percentage yield and the annual rate of interest should be displayed with equal prominence (same-sized type).
- o When advertising certificates of deposit or any account with a maturity of less than one year, either omit reference to the annual percentage yield or state clearly that the yield is based on compounding of the amount at the stated interest rate for a year and that the actual yield will be less, based on the length of time money remains in the account.

- Do not use the term "profit" when referring to interest paid on deposits.
- When advertising time deposits with an initial rate effective for a period of a few months and a lower rate that will be effective for the remaining term of the time deposit, both rates should be stated in type of equal size. Also, the ad must include a statement of the annual yield. (The staff of the Federal Reserve Board has advised member banks not to advertise for a time deposit stating an annual rate of simple interest in excess of the average effective annual yield.)
- Advertisements for Individual Retirement Accounts should not refer to contributions to such accounts as "tax-free" or "tax-exempt." In fact, federal income taxes on contributions to and earnings on IRAs are deferred.
- Advertisements for time deposits where more than one rate is paid are not considered misleading if each rate is stated in type of equal size together with a clear statement as to the length of time each rate is effective. Such ads also must include a conspicuous statement of the average effective annual yield for the deposit.

Following are examples of "right" and "wrong" rate advertisements.

ATTACHMENT 2

GIANT
RATES

EARN A
JUMBO PROFIT

11.00% 12 Months*
10.50% 180 Days**
10.00% 90 Days

Minimum Deposit Required
FOR DETAILS, CALL 555-0000.

*Per annum simple interest—rate good until May 19
**Variable rate adjusted monthly.

WRONG AD

123 Main Street,
Anytown, U.S.A.

ANNOUNCING A NEW MARKET RATE

SPECIAL OFFERING
90-DAY C.D.

10.00%	**10.47%**
Annual Rate of Simple Interest	Annual Percentage Yield*

- $2,500 Minimum.
- Compounded and credited monthly.
- Deposits insured up to $100,000 by the Federal Deposit Insurance Corporation.
- Substantial interest penalty required for early withdrawal.
- This special offer is good only until October 10, so act now.

RIGHT AD

Branches at Town Center Mall
Main Street Plaza and
Country Club Road

CALL 1-800-555-1000 OR COME IN TO YOUR NEAREST BANK BRANCH FOR DETAILS.

*The yield on this account is based upon monthly compounding at the stated interest rate for a full year. The actual yield may be less, based on how long your money stays in the account.

"RIGHT" ADVER EMENT

- Prese the annual percentage yield and the annual rate of simpl nterest clearly and with equal prominence.
- Point ut the minimum deposit required..
- Expla when the account is compounded and credited.
- Discl s how the yield is determined.
- State he duration of the special offer.
- Inclu conspicuous notice that a substantial interest penal is required for early withdrawal.

"WRONG" ADVER EMENT

- Shows terest rates for three separate accounts with no menti of annual percentage yields.
- Uses phrase "per annum simple interest," which is jargon for erest compounded annually." Thus, the yield and the rate these accounts would be identical, but the average custo would not know it.
- Prom tly displays the term "profit," which may not be used referring to interest paid on deposits.
- State nly that "minimum deposit required." Does not indic amount required.
- State n inappropriately small type that the 10.50% rate show variable and will be adjusted monthly. No indi on is given of subsequent monthly rates or of the basi the monthly adjustments.
- Does t include a clear notice that a substantial interest pen is required for early withdrawal.

Therefore, we assume that the uniform yield formula will be adopted with only minor modifications.

Not only does the SEC strictly regulate mutual fund advertising, but all mutual fund advertisements and sales literature are subject to regulatory review, not only by the SEC, but the NASD, the self-regulatory organization of the brokerage industry and by a number of the States.

In contrast to the comprehensive system of advertising regulations to its mutual funds, the regulation of bank products is nominal at best. Moreover, unlike the active role taken by the SEC, the attitude of bank regulators insofar as consumer disclosure is concerned can best be characterized as caveat emptor.

Indeed, in 1982 the Federal Home Loan Bank Board refused to adopt proposed advertising controls on the grounds, and I quote, that "there is no need to impose requirements designed to protect investors from their own lack of due diligence."

I would remind you, Mr. Chairman, that in 1933 when President Roosevelt signed the Securities Act to which mutual funds are subject, he said at the ceremony of signing the bill that "This changes the law with respect to securities from caveat emptor to caveat vendor," and I think the SEC has lived up to those words since that time.

I think the Congress is well justified in taking steps which the bank regulators themselves have proven reluctant to take. We therefore strongly endorse S. 1507.

We also respectfully suggest that the bill be amended in two respects.

First, to further the goal of regulatory uniformity and to provide the public with comparable information, we suggest an amendment to require the Federal Reserve Board and the SEC to consult for the purpose of coordinating and harmonizing their regulatory efforts.

I think, Mr. Chairman, that an amendment along these lines gets this red herring off the stage and I assume that my colleagues on this panel representing the ABA and the U.S. League will now wholeheartedly and unreservedly endorse the bill as we do.

Second, we believe that advertising of various types of bank collective investment funds should be subjected to the same advertising restraints as mutual funds.

I should conclude, Mr. Chairman, by expressing my gratitude for being here today, but I really can't do that. You have summoned me from the shores of Bantam Lake in beautiful Morris, CT, and I will return there by the earliest available means of transportation at the conclusion of this hearing, but we do appreciate this opportunity to express support for the bill and we do want to take a constructive attitude. We see the need for uniformity.

Thank you.

[The complete prepared statement of David Silver follows:]

WRITTEN STATEMENT OF THE
INVESTMENT COMPANY INSTITUTE
BEFORE THE
SUBCOMMITTEE ON CONSUMER AFFAIRS
OF THE
SENATE BANKING, HOUSING AND URBAN AFFAIRS COMMITTEE
REGARDING
S. 1507

AUGUST 5, 1987

Good afternoon. My name is David Silver, and I am president of the Investment Company Institute. The Investment Company Institute is the national association of the American mutual fund industry. Its membership includes over 2,000 open-end investment companies, or mutual funds, which account for over 90% of industry assets, with over 29 million shareholders.

I. INTRODUCTION

The Institute appreciates being given the opportunity to testify concerning S.1507, the Truth in Savings Act. The mutual fund industry, long subject to disclosure and advertising regulations more stringent than those imposed on other types of financial institutions, wholeheartedly supports legislation that would improve the quality of information available to the investing public. In fact, this bill answers a long-standing need: to establish a framework for regulating advertising of certain bank products that approximates the stringent regulations that apply to mutual funds. Further, we believe that the bill can be improved to provide an even broader framework to harmonize the regulation of advertising of bank savings and investment products with the regulation of SEC-registered products, most notably mutual funds. The investing public would be the beneficiary of reasonably comparable advertising standards among these products. In this spirit, we would propose two amendments to perfect this already excellent bill. However, even without these amendments, the bill would make a start in placing some of the restraints to which mutual fund advertising is already subject on bank products.

We would start by giving the Subcommittee some background information on how mutual fund advertising is regulated, and then explain our two amendments to assist this Subcommittee in attaining its goal of establishing an effective regulatory framework.

II. SEC REGULATION OF MUTUAL FUND ADVERTISING

Mutual funds are subject to a comprehensive system of regulation under the federal securities laws. Unlike other securities, shares of mutual funds are continuously registered under the Securities Act of 1933 and therefore are subject to the Act's disclosure and updating requirements on a continuing basis. In addition, distributors of mutual funds are regulated as broker-dealers by the Securities and Exchange Commission (SEC) under the Securities Exchange Act of 1934 and are subject to regulation by the National Association of Securities Dealers, Inc. (NASD), a self-regulatory organization under SEC jurisdiction. Moreover, investment advisers to mutual funds must be registered with the SEC under the Investment Advisers Act of 1940. Finally, mutual funds themselves, unlike almost all other companies, must register with the SEC under the Investment Company Act of 1940, a highly detailed regulatory statute.

A. The Securities Act of 1933 Mandates Full Disclosure by Mutual Funds

The Securities Act of 1933 sets forth a comprehensive disclosure system by issuers of securities. Because mutual funds continuously offer their shares to the public, disclosures by mutual funds are always subject to SEC disclosure and advertising regulation under the Securities Act.

There are three types of disclosure documents permitted to mutual funds under the Securities Act. The most fundamental is the prospectus, a comprehensive disclosure statement that must be provided to all investors. Second, mutual funds may do limited kinds of advertising which solicit investors to request copies of the prospectus. Finally, mutual funds may use "supplemental" sales literature, that is sales literature that supplements the information in the prospectus. Supplemental sales literature must be preceded or accompanied by the prospectus.

The SEC has adopted specific rules for mutual funds in all three areas of communication.

1. Prospectuses

The SEC has adopted a specialized registration form, Form N-1A, to govern the form and contents of mutual fund prospectuses. Among other things, the form requires prospectus disclosure by mutual funds of all fees and of how the fund calculates performance if it advertises performance. Specific disclosures in the form are always under review. For example, the SEC currently has out for comment proposals concerning the disclosure of fees and performance information by mutual funds.

2. Advertisements

Mutual fund advertisements may take one of two forms. First, a mutual fund may use a tombstone advertisement that merely contains identifying information and does not contain any yield or performance information.[1] Second, Rule 482 under the Securities Act permits mutual funds to use as advertisements "omitting" prospectuses. Under the rule a mutual fund may use an advertisement that contains yield or performance information if the information is based on information in the fund's prospectus. Such advertisements are subject to stringent liability standards and may only solicit requests for the fund's prospectus, not purchases of fund shares.

3. Supplemental Sales Literature

From 1950 until 1979 mutual fund use of performance information in supplemental sales literature was subject to a very detailed SEC Statement of Policy. In 1979 the SEC repealed the Statement of Policy and adopted Securities Act Rule 156. Rule 156, which also applies to mutual fund advertisements, sets forth general anti-fraud principles and provides guidance in applying those principles.

In addition to SEC regulation of mutual fund advertising, the NASD also regulates mutual fund advertising by broker-dealers. The NASD has adopted guidelines concerning appropriate disclosures of mutual fund performance and other information.

B. The SEC is a Vigorous Regulator

SEC regulation of mutual fund advertising practices is not static but is constantly evolving to meet changing conditions and investor needs. Over the last 10 years, during the period of the greatest growth of the mutual fund industry, the SEC has taken an active role not only in enforcing existing regulations, but in amending existing rules and developing new provisions to deal with new mutual fund products.

For example, in 1980, the SEC addressed advertising by money market mutual funds, the mutual fund product competing most directly with bank deposits. In that year, the SEC amended Rule 482 to require all money market funds which advertise yield to use a single, uniform method for computing yield. In 1983 the rule was amended again to add a single, uniform method of computing effective (or compound) yield for money market funds. These two methods for calculating yield are the only methods a money market fund may use for computing yield figures used in an advertisement. Moreover, a money market fund may not advertise an effective yield unless it also includes in the same advertisement its simple yield.

More recently there has been a sharp increase in consumer interest in mutual funds investing in bonds and other long-term debt instruments. In response, an industry group formed by the Institute reviewed income fund advertising, and identified two major issues concerning yield advertising by income funds: (1) uniformly calculating yield and (2) insuring adequate disclosure to investors of market risk. On March 11, 1986 the Institute submitted to the SEC staff a comprehensive proposal for rulemaking that addressed both of these issues. It set forth a uniform method of computing yield for income mutual funds. The proposal also addressed the issue of market risk by requiring yield advertisements to disclose that both yield and share price will fluctuate and, in order to illustrate share price fluctuation, the beginning and ending per-share net asset values for the preceding twelve months.

In September 1986, the SEC proposed extensive new rules to govern advertising by income mutual funds (as well as advertising by funds investing in equities). Although the industry and the SEC staff are in disagreement over portions of the proposed rules, the proposed rules include a yield calculation formula for income mutual funds that is substantially the same as the formula suggested by the Institute. The uniform yield formula for income funds is almost certain to be adopted with only minor revisions.

C. Ongoing Review of Mutual Fund Advertisements and Sales Literature

Not only does the SEC strictly regulate the contents and use of mutual fund advertising, but all mutual fund advertisements and sales literature are subject to regulatory review. First, mutual fund advertisements and sales literature must be filed with the SEC, which reviews such communications as part of its regular process of inspecting mutual funds.[2] Second, all mutual fund advertisements and sales literature used by NASD member firms (this includes almost all mutual fund literature) must be submitted to and reviewed by the NASD.[3]

---

[1] Securities Act Rule 134 governs the content of tombstone advertisements.

[2] Section 24(b) of the Investment Company Act of 1940 requires mutual funds to file advertisements and sales literature with the SEC. The SEC has proposed to exempt advertisements and sales literature filed with the NASD from the filing requirement. However, such materials would still be reviewed by the SEC as part of the inspection process.

[3] Article III, Section 35 of the NASD Rules of Fair Practice govern filings.

III. REGULATION OF BANK ADVERTISING IS SORELY LACKING

In contrast to the long-standing and comprehensive system of advertising regulation to which mutual funds are subject, the regulation of bank products is nominal at best. Moreover, unlike the active role taken by the SEC, the attitude of bank regulators can better be characterized as "caveat emptor."

Members of Congress have long recognized the need for greater regulation of bank advertising. Almost 10 years ago, in 1978, Chairman Proxmire expressed concern that banks run advertisements for their collective investment funds for retirement plans completely free from SEC advertising regulation under the federal securities laws:

> "It's astonishing that they can do this and the SEC has no authority, no jurisdiction, and they can do that in competition of course with your [the mutual fund] industry."4/

Chairman Proxmire also stressed the competitive inequities which result from subjecting mutual fund advertising to regulation under the federal securities laws, while exempting bank advertising from these laws:

> "It just doesn't seem to be logical at all. Either what the SEC is doing in restraining the [mutual fund] industry is wrong, which I think it is not -- I think it's right -- or banks should be restrained on the same basis."5/

Congress is well justified in taking steps which the bank regulators themselves have proven over time to be unwilling to take.

For example, during the late 1970s depository institutions developed a new instrument in the form of a short-term, uninsured debt security, the retail repurchase agreement ("retail repos"). The development and proliferation of retail repos was encouraged by the Comptroller of the Currency, who issued guidelines concerning the issuance of these products. These guidelines urged depository institutions engaged in marketing these products to disclose all material information concerning the repos to customers.

4/ Hearings on S. 72 Before the Senate Committee on Banking, Housing and Urban Affairs, 95th Cong., 2d Sess. (1978), at 348.

5/ *Ibid*.

However, this advice was not faithfully followed. In 1981, Rep. Benjamin Rosenthal, then Chairman of the Commerce, Consumer, and Monetary Affairs Subcommittee of the House Committee on Government Regulations, wrote to the Chairman of the Federal Home Loan Bank Board (FHLBB) to criticize savings and loan associations' marketing programs for retail repos as "seriously misleading and deceptive."6/

Despite this Congressional concern, the FHLBB subsequently adopted regulations that abandoned essential consumer protections.7/ The FHLBB justified its actions reducing consumer protection, in part, as follows:

> The proliferation of short-maturity retail repurchase agreement programs is a strong indicator of the increased sophistication among retail repurchase agreement investors, who balance an investment's rate of return against its relative liquidity. In such a highly competitive climate, there is no need to impose requirements designed to protect investors from their own lack of due diligence." (Emphasis added.)8/

The Federal Reserve Board has been less cavalier, but no more effective, with respect to bank advertising of Individual Retirement Account deposits. In March 1984, in response to IRA deposit advertising practices that a member of the Board characterized as "scandalous," the Board issued a Statement of Policy concerning certain misleading advertising practices.9/ At the same time, the Board issued for public comment a proposal to amend Regulation Q, the regulation governing advertising of interest on deposits, to incorporate the principles set forth in the Statement of Policy.10/

However, despite this hopeful initiative, no final rules have ever been adopted by the Board.

6/ Letter from Benjamin S. Rosenthal, Chairman, Commerce, Consumer and Monetary Affairs Subcommittee of the House Committee on Government Operations, to Richard T. Pratt, Chairman, Federal Home Loan Bank Board, dated July 29, 1981.

7/ For example, the FHLBB did not adopt proposals to require disclosure in S&L advertisements that repos are not guaranteed by the U.S. Government. Federal Home Loan Bank Board, May 20, 1982.

8/ *Ibid*.

9/ 49 F.R. 11620, March 27, 1984.

10/ 49 F.R. 11642, March 27, 1984.

IV. THE PROPOSED LEGISLATION REPRESENTS A GOOD BEGINNING

Given the failure of the bank regulatory authorities to adopt advertising and disclosure standards similar to those imposed by the SEC on mutual funds and other issuers of securities, it is essential that Congress act. As noted by Rep. Lehman, in discussing H.R. 176, the companion bill to S. 1507,

> . . . similar instruments, especially those offered by securities firms, come under stringent advertising and disclosure requirements which are heavily regulated and enforced by the Securities and Exchange Commission. These advertising regulations are more restrictive and a proposed new rulemaking would standardize the computation of mutual fund performance data in advertisements and disclosures. Clearly, in the absence of similar advertising registration requirements and performance rulemaking and standardization among the banking regulatory agencies, some legislative relief to provide uniform and clear disclosure by financial institutions is appropriate.[11]

We therefore strongly endorse the enactment of S. 1507. We also respectfully suggest that the bill be amended in two respects.

First, to further the goal of regulatory uniformity, we suggest an amendment, attached as Exhibit B, to require the Federal Reserve Board and the SEC to consult for the purpose of coordinating and harmonizing their regulatory efforts. Given the SEC's long experience in regulating advertising, we feel that its perspective and advice will benefit the Board in its efforts to effect the intent of Congress.

Second, the bill as presently drafted only addresses bank advertising relating to deposit accounts, and fails to deal with bank advertising for banks' collective investment funds for retirement plans. This problem was identified by Chairman Proxmire in 1978, and subsequently has been the subject of Congressional testimony by former SEC Chairman Williams[12], Congressional testimony by former SEC Chairman Shad[13] and was discussed in a recent GAO Report to Members of Congress.[14] We therefore recommend the adoption of an amendment (attached as Exhibit C) to require the Federal Reserve Board to adopt regulations in this area.[15]

---

[11] Cong. Record - House, H. 5760, June 29, 1987.

---

[12] In 1979, SEC Chairman Williams called attention to the fact that in 1970 Congress exempted bank collective investment funds from regulation under the federal securities laws at a time when regulations of the Comptroller of the Currency prohibited merchandising and advertising, but that:

> "In a sharp departure from this historical setting, however, regulations of the Comptroller of the Currency were recently amended to provide that general advertising prohibitions -- which embodied the policies underlying the exemption provided in the Securities Act -- are no longer applicable to collective investment trust funds maintained by banks for corporate pension funds. As a result, many banks have begun to market interests in those trust funds aggressively through general advertising about the investment performance of those corporate pension trusts. Although these bank trust funds compete with other collective investment media such as investment companies and insurance company separate accounts, which generally are subject to the registration provisions of the Securities Act, individual plan participants in the corporate pension plans purchasing interests in bank trust funds may be denied the protection afforded under the Securities Act to which they would be entitled if their corporate pension plan administrators had chosen to invest in these competing media."

Hearings Before the Subcommittee on Financial Institutions Supervision, Regulation and Insurance of the House Committee on Banking, Finance and Urban Affairs on H.R. 1539, H.R. 2747 and H.R. 2856 (1979), at 17.

[13] Hearings Before the Senate Committee on Banking, Housing and Urban Affairs on the Financial Institutions Restructuring and Services Act of 1981, 97th Cong., 1st Sess., Pt. II at 898.

[14] "Functional Regulation: An Analysis of the Two Types of Pooled Investment Vehicles," United States General Accounting Office, May 1986.

[15] A more comprehensive approach would be the enactment of legislation, suggested by former SEC Chairmen Williams and Shad, which would subject bank collective investment funds to regulation under the federal securities laws.

We would note, however, that even after enactment of the legislation, including our two suggested amendments, banks will not be subject to as stringent advertising and disclosure requirements as are mutual funds.[16] For example:

> First, the bills would permit banks to "sell off" advertisements. That is, bank advertisements containing yield figures would be permitted to solicit the opening of accounts. Therefore, a customer could clip a coupon from a bank ad, send a check and make an investment in a bank deposit without receiving a disclosure document. In contrast, mutual fund advertisements may only solicit requests for a mutual fund's full prospectus and may not solicit immediate investment in the fund. A mutual fund can not "sell off" an advertisement.
>
> Second, unlike the system of SEC and NASD review of mutual fund advertisements and sales literature, the bill does not provide for even one layer of regulatory review of bank advertisements.
>
> Third, it is unclear whether the bill would require the Federal Reserve Board to adopt a uniform formula for the calculation of yield or whether the Board could permit variations in the calculation. In contrast, SEC Rule 482 sets forth uniform formulae for computing money market fund yields.
>
> Fourth, the bill would place a low "cap" on a depository institution's liability for non-compliance; no such cap exists in the federal securities laws.

We suggest that Congress consider these matters in connection with this or future legislation.

We greatly appreciate the opportunity to testify before you and express our strong support of S. 1507.

---

[16] A detailed comparison of SEC requirements governing mutual fund advertising to the proposed requirements of S. 1507 is attached as Exhibit A.

EXHIBIT A

H.R. 176/S. 1507 Truth in Savings Act

A. Any advertisement containing performance information must contain

1. Annual Percentage Yield (defined term to be calculated by method to be prescribed by FRB)
    - a. period it is in effect
    - b. minimum account balance/time requirements necessary to earn this yield
    - c. must be given greater prominence

2. Ads containing more than one yield
    - a. minimum account balance for each
    - b. figures and minimum balances must be in close proximity and given equal prominence

3. Minimum initial deposit to earn advertised yield if greater than usually required

4. Simple interest figure

5. Caveat that fees/other conditions could reduce yield

SEC Requirements - Mutual Funds

A. Ads containing performance information are governed by rule 482 under the Securities Act of 1933

1. These ads are considered to be "prospectuses"
    - a. can contain only information the substance of which is in full prospectus

2. Money Market Fund ads including performance data must include
    - a. current yield figure calculated according to standard SEC formula
    - b. effective yield figure can only be used in conjunction with current yield figure and calculated according to standard SEC formula
    - c. The ad must identify the base period for each performance figure and if both figures are used the base period must be the same

3. Non-money market fund ads including performance data must include (proposed):
    - a. Total return figures for each of last 5 years, plus interim period since end of last year, computed under standard SEC formula
    - b. income funds (as defined in Rule 482) may also include current yield figure, calculated according to standard SEC formula and mandatory accounting rules
    - c. tax-exempt income funds (as defined in rule 482) can also include a "tax-equivalent yield" figure
    - d. all performance figures must be given equal prominence

Senator DODD. Thank you.

Well, if you had been a decent constituent you would have invited us to hold the hearings in Bantam Lake and all of us could have been there with you. [Laughter.]

Mr. SILVER. We've had to use a blanket every night last week. [Laughter.]

Senator DODD. That's a very nice spot, too, and we thank you for coming down and I can appreciate your wanting to get back.

I have just a series of questions for each of you. What I would like to do is sometimes I ask a question of one and others have a comment on it. So I'm interested in some of the dynamics that occurs with all four of you there.

Briefly for you, Mr. Pitt, in your testimony you state that the Bank Board regulations require that S&L's disclose the annual rate of simple interest, the percentage yields based upon 1 year and percentage yields based upon more than 1 year.

METHOD OF BALANCE CALCULATION

I wonder, do you think that these requirements mandate the method of balance calculation?

Mr. PITT. I do not, and I think that what we would continue to support is clear disclosure of the method by which the individual institution does calculate its balance, whether it's day of deposit to day of withdrawal or whatever other method, and that clearly needs to be distinguishable and in full disclosure so that the customer, depositor or saver knows exactly how that calculation is going to be made.

Senator DODD. Furthermore, are you recommending that money market funds disclose that the investor has no absolute right to a return of principal?

Mr. PITT. We think that clearly needs to be put forth because an investment in a mutual fund is clearly an equity investment and the principal is at risk, and that needs to be fully disclosed. Yes, we support that.

Senator DODD. I thought maybe the absence of any mention of that means you had some other additional thoughts on that.

Mr. PITT. No, absolutely not.

Senator DODD. Mr. Fox, again we welcome you here and recognize that you're having two or three hats on here today, but with a common interest.

I wonder if you could tell us what percentage of banks use the low-balance and first-in and first-out balance calculation methods? Do you have that information?

Mr. FOX. I don't have any of my own information. There is a publication put out by the American Bankers Association, the 1985 Retail Deposit Services Report.

Senator DODD. Well, maybe we can get Mr. Shipman. Do you know the answer to that?

Mr. SHIPMAN. It's a very, very small percentage.

Senator DODD. A ball park——

Mr. SHIPMAN. Less than 10 percent.

Senator DODD. Less than 10. I think we might like to have that, if it's less than 10 or——

  - e. legend stating figures represent past performance, that investment return and principal will fluctuate and that as a result payment upon redemption may be more or less than original cost
  - f. disclsoure of fees and sales charges, including maximum amount of fee or charge, whether performance figure reflects deduction of such fees or charges, and if not, that fee acts to reduce quoted performance
  - g. disclosure of measuring period for each performance figure
  - h. tax-exempt income funds must disclose tax-exempt status at state, local and federal level

4. All ads must state conspicuously from whom full prospectus can be obtained, and warn investors to read prospectus before investing

5. (Proposed) Performance data can not be more than 30 days old at date of publication

H.R. 176/S. 1507 Truth in Savings Act	SEC Requirements · Mutual Funds
B. Broadcast/Electronic/Outdoor Media 1. Advertisements utilizing such media can be exempted by FRB if such disclosure would be "unduly burdensome"	B. Broadcast/Electronic/Outdoor Media included
C. Antifraud Provisions 1. Cannot refer to account as "free" or "no cost" if fees imposed 2. General antifraud "misleading" standard	C. Antifraud provisions 1. Since 482 ad is a "prospectus," failure to include material information, or inclusion of misleading statements, subjects fund to civil liability to shareholder, who can recover amount of investment, less income derived therefrom, or damages (Securities Act Sec. 12(2)) 2. General antifraud "misleading" standard (Securities Act Rule 156)

D. Accompanying Disclosure Requirements

1. Account Schedule (FRB to develop regs) to include
    - a. information on fees and charges
    - b. information on interest rates including annual percentage yield and simple interest, period rates in effect, frequency of compounding, balance on which yields based, minimum account balance/time requirement to earn rate, early withdrawal penalties
    - c. other information necessary to make clear to consumers (as determined by FRB)
    - d. easy-to-read/understandable format

2. Distribution of Disclosure Documents
    - a. Must be delivered to current accountholders
    - b. Must be made available upon request
    - c. Must be given to potential customers prior to opening new account or mailed within 10 days of initial deposit if depositor not present when account established

3. Forms
    - a. FRB to promulgate model forms and subject to public comment process

D. Accompanying Disclosure Requirements

1. Investors must receive a full statutory prospectus
    - a. Form N-1A promulgated by SEC
    - b. includes information on fees and charges
    - c. must be updated annually (any material change requires immediate updating)
    - d. instructions specify clear form and language must be used
    - e. further, in-depth discussions of performance information, including actual performance figures, contained in Statement of Additional Information, must be given to investor on request
    - f. if advertising yield or total return, prospectus must describe methodology used to compute yield or total return

2. Investors cannot invest by sending ad coupon to fund

3. Type size must meet required minimum (Rule 420)

4. Any other communication including performance data (other than 482 ad) must be preceded/accompanied by full prospectus

H.R. 176/S. 1507 Truth in Savings Act	SEC Requirements - Mutual Funds
E. Discretionary authority given to FRB to modify statutory disclosure requirements with respect to certain accounts.	E. SEC can amend rules and forms
F. Exemptions 1. FRB may grant adjustments, differentiations and exceptions	F. In theory, SEC can grant exemptions

H.R. 176/S. 1507 Truth in Savings Act

G. Liability for non-compliance
  1. Civil liability
    a. actual damages
    b. liability limited to maximum of $1,000, minimum of $100
    c. for class action, liability limited to lesser of $500,000 or 1% of net worth of depository institution
    d. costs and attorney's fees awarded to successful plaintiff

  2. Bona Fide Errors
    a. Depository institution not liable if non-compliance due to bona fide error

SEC Requirements - Mutual Funds

G. Liability for non-compliance
  1. Civil liability
    a. amount of investment minus income derived therefrom
    b. actual damages
    c. derivative suits permitted on behalf of all investors in a fund

  2. Liable Despite Bona Fide Error.

H. Oversight
  1. Filing requirements
    a. SEC: 5 copies must be filed simultaneously first use (proposed: only if not filed with NASD)
    b. SEC: broadcast ads must be filed prior to first use
    c. NASD: must be filed within 10 days of first use
    d. State: 9 states require filing; 6 of these require filing prior to use

  2. Copies of ads must be maintained in mutual funds' record file and are subject to review upon SEC or NASD examination

  3. NASD requires signature of registered principal prior to use

EXHIBIT B

The Board and the Securities and Exchange Commission shall consult for the purpose of coordinating and harmonizing the regulations adopted under this Act and those adopted under the authority of the Securities Act of 1933, the Securities Exchange Act of 1934, the Investment Company Act of 1940 and the Investment Advisers Act of 1940 to assure that consumers of financial services and products receive a parity of disclosure and to create a fair field of competition between financial institutions subject to this Act and the laws administered by the Securities and Exchange Commission. The Board and the Securities and Exchange Commission shall file a joint report yearly to the committees with oversight jurisdiction as to the progress they have made in achieving the purposes set forth in this paragraph.

EXHIBIT C

The Board shall adopt regulations relating to advertising and disclosure by depository institutions with respect to collective investment funds maintained by such institutions and consisting solely of assets of retirement, pension, profit sharing, stock bonus or other trusts which are exempt from federal income taxation under the Internal Revenue Code. In adopting such regulations, the Board shall consider regulations adopted by the Securities and Exchange Commission under the authority of the Securities Act of 1933, the Securities Exchange Act of 1934, the Investment Company Act of 1940 and the Investment Advisers Act of 1940 with respect to advertising and disclosure by companies registered under the Investment Company Act of 1940.

Mr. **Shipman**. We can make that available to the staff if you would like that.

Senator **Dodd**. Could you. That would help us.

[The information referred to follows:]

AMERICAN
BANKERS
ASSOCIATION

1120 Connecticut Avenue, N.W.
Washington, D.C.
20036

GOVERNMENT
RELATIONS:
RETAIL BANKING

DIRECTOR
Frank P. Curran
202 663 5436

September 25, 1987

Mr. Peter Kinzler
Minority Counsel
Senate Banking Committee
534 Senate Dirksen Office Building
Washington, D.C. 20510

Dear Peter:

This is in response to David Moses' recent phone conversations with Betsy Dribben of our staff, and Jack Shipman who testified on our behalf on Truth-in-Savings legislation. We are happy to provide answers to several questions raised during the hearings.

1. Information compiled from the ABA's 1986 Retail Deposit Service Report indicates the percentage of banks utilizing low balance methods of calculation is under five percent of banks in all size categories.

2. Concerning the investable method of calculation, the Bank Marketing Association surveyed 3,000 banks this summer to determine to what degree the investable balance method of calculation for consumer accounts was utilized in the industry. Of the 1,100 responding banks, approximately 13 percent indicated they offered a consumer savings product which was based on the investable balance method of calculation.

   The investable balance method of calculation for consumer accounts appears to have been used initially after the implementation of the Monetary Control Act of 1981. However, most banks which decided to use it did so beginning in the early part of 1987. This coincides with the final implementation phase of the reserve requirements set forth in the Monetary Control Act.

3. David Moses also requested that we provide statistics on money market deposit accounts, interest bearing checking accounts, and money market mutual funds. The figures we have available (all deposits are in billions) are as follows:

AMERICAN
BANKERS
ASSOCIATION

CONTINUING OUR LETTER OF

SHEET NO

Money Market Deposit Accounts (as of May 1987)[1]

Community Banks	$368.8
Thrifts	188.3
TOTAL	$557.1

Money Market Mutual Funds (as of July 1987)[2]

TOTAL	$239.2

Other Checkables* (as of May 1987)[3]

Community Banks	$171.6
Thrifts	77.9
TOTAL	249.5

1. Federal Reserve Board H-6 Release.
2. ICI Figures.
3. Federal Reserve Board H-6 Release.

*Other checkables include NOW accounts and Automatic Transfer Services (ATS)

We did not have actual numbers of money market deposit accounts and checking accounts available.

We are also taking the liberty of enclosing a recent news clip which you may not have seen. We believe it provides further indication that consumers need Congressional assistance in sorting out advertised information on mutual funds.

Again, we hope the enclosed information will be of assistance to you. Please give me a call if you have any further questions.

Sincerely,

F. R. Curran

Frank Curran

Enclosures

Senator DODD. Mr. Fox, you've indicated that you would strongly like to standardize the balance calculation method. If we do that, which method would you like to see us standardize?

Mr. FOX. I think there are three methods that essentially provide the same outcome and, more importantly, meet the consumer's expectation of what is going on in an account, and those would be any sort of average balance method where the average balance over the period for which interest is being calculated is taken, or a day-of-deposit to day-of-withdrawal as illustrated in the charts, or any daily balance method which would occur when interest is compounded and credited daily on the full balance.

What all three of those techniques have in common is that they meet the consumer's expectation that the consumer receives interest on the full amount on deposit in the account, and I think legislative language that spells that out would still permit any of those three techniques and would still allow variances in compounding and crediting, which we don't object to because those variances, first of all, can be reflected accurately in the annual percentage yield that's disclosed to consumers and, second, are legitimate variations that don't hide anything of importance to the consumer.

Senator DODD. Now just quickly you, Mr. Shipman, what percentage of banks utilize those three methods?

Mr. SHIPMAN. This is a 90-day passbook type of calculation. What we are dealing with in our reference technology today, the great major of banks provide a monthly statement of their savings accounts. So this type of example of averaging over 90 days is just not prevalent in the industry at all today.

We find that a great deal of it is the date-of-deposit to date-of-withdrawal, and again it's in the——

Senator DODD. That's the most popular?

Mr. SHIPMAN. Yes, sir.

Senator DODD. What percentage of banks use that?

Mr. SHIPMAN. Mr. Curren just informed me. It's 85 to 87 percent, in that range.

Senator DODD. All right. And what about the daily balance method?

Mr. SHIPMAN. Well, I think that's in the same—they're combined, as I referred to it. One of the two is in the 90 percent bracket if you add that back in. It's only the two that are predominant, date-of-withdrawal or some average balance.

Mr. FOX. Mr. Chairman, unless there has been a change in the last 2 years, those numbers simply aren't reflected in the ABA's own 1985 report. If you look at the frequency of compounding on passbook savings deposits, they don't have a total figure for the entire industry because it's broken down by assets.

Senator DODD. What are you reading from, Mr. Fox?

Mr. FOX. I'm reading from the 1985 Retail Deposit Services Report published by the American Bankers Association. Quarterly compounding is used on passbook savings deposits by between 37 and 48 percent of different banks, depending on asset size, another 4 to 9 percent use semiannual compounding and some even use annual compounding. In fact, only among the smaller banks do a majority use daily compounding and another 4 or 5 percent at all asset sizes use monthly compounding.

The ABA recently announced its own survey that indicates that 14 percent of all banks use the investable balance method on at least some of their accounts. Clearly daily methods are the most common, but they are by no means used overwhelmingly in the banking industry.

Mr. **Shipman**. That is an older report, as he reflected. It's 1985 data. It was published in 1985 and it was really collected probably in 1984. Again technology has replaced. He is referring to passbook savings, and when you get into a statement savings account it really dictates that you use the average daily balance or the date-of-deposit and date-of-withdrawal. But we'll be happy to furnish the chairman that information on money market type accounts, the checking accounts that we're paying interest. With the deregulation, those are really the result of deregulation of the industry because we've developed new product.

[The information referred to follows:]

TABLE 30
PERCENTAGE OF BANKS USING SELECTED METHODS FOR COMPUTING INTEREST ON SAVINGS DEPOSITS

	Asset Size (In Million Dollars)				
	Less Than 50	50-100	100-500	500-1,000	1,000 or More
Day of deposit to day of withdrawal	48.1	60.0	50.0	68.3	54.9
Day of deposit to end of interest period	10.1	10.7	14.1	9.8	11.3
Low balance for interest period	2.5	-	1.8	2.4	-
Low balance for month	2.5	1.3	1.8	-	1.4
Average balance for the month	8.9	8.0	4.1	4.9	8.5
Average balance for interest period	12.7	8.0	13.5	4.9	4.2
Other*	15.2	12.0	14.7	9.7	19.7

*Includes combination of methods

TABLE 31
PERCENTAGE OF BANKS USING SELECTED METHODS FOR COMPUTING INTEREST ON NOW ACCOUNT DEPOSITS

	Asset Size (In Million Dollars)				
	Less Than 50	50-100	100-500	500-1,000	1,000 or More
Day of deposit to day of withdrawal	34.6	33.4	33.0	53.7	41.0
Day of deposit to end of interest period	5.1	7.2	10.7	9.8	7.4
Average balance for month	25.6	24.6	27.2	14.6	16.2
Average balance for interest period	10.3	14.5	9.5	4.9	5.9
Low balance for the month	2.6	4.3	0.6	2.4	1.5
Low balance for interest period	2.6	3.0	1.2	-	1.5
Other*	19.2	13.0	17.8	14.6	26.5

*Includes combination of methods.

Senator Dodd. Well, let me ask you this. If you're getting a number, and let's say we're close. Let's say that 85 to 90 percent are using one method and you've got about 10 percent using three other methods or more. Why not just come up with one method? It would seem to me it would simplify things dramatically if the vast percentage of banks are using it anyway and why not proceed along that line?

Mr. Shipman. I think we are talking about product development versus the informed consumer. The bill is really stating to the consumer because it's still the world of a competitive environment, and if I have to display that the APR is 6 percent and the APY is less than that, significantly less, and that's what is going to happen in the real world, you're not going to get anybody to invest in that type of an instrument. And, besides, we give full disclosure at the time they open the account as to how it's done.

But from all the colleagues that I've talked to, we're supportive and we really think that the answer is to show both of those yields, the APR and the APY. The consumer has to then react to what he thinks is the investment for him.

Mr. Fox. Mr. Chairman, in the four examples on the chart here, every one of those four examples has an APR of 6 percent and an APY of 6.14 percent, every single one of them, and I submit that there is no way a consumer would understand in looking at those four examples that those percentage rates would result in such radically different dollar amounts, and that's what the consumer is concerned about. The consumer can't spend 6 percent, but the consumer can spend $75.

Senator Dodd. We can come back, but I'm just interested in getting both of you to comment on these things rather than just have to go through a whole series of them.

One of the tricky questions, Mr. Fox, that I find of mandating disclosures, I don't think I'm an abnormal consumer and I can be overwhelmed by labeling. I don't know what number of lines it is that I tune out on, but I find that if I look at something that has too much on it, I don't read any of it, and if it's clearly a few lines or whatever, I'm more inclined to kind of focus on it.

And obviously our goal here is to try and put in disclosures that consumers will read. I mean if we put disclosures that one is going to look at, I mean obviously you and I feel better, but the consumer necessarily isn't more enlightened in terms of the choices.

Do you think that we need to require the disclosure of an annual rate of simple interest in advertisements if we require the disclosure of annual percentage yields, for instance? Should we make some choices in some of these things?

Mr. Fox. I think many consumers do find the annual rate of simple interest to be a more meaningful figure than the annual percentage yield. The reason is that many of the accounts we're looking at are transaction accounts where there is account activity and the funds are not in fact left in the account over the course of a year to accumulate interest and to build up that higher figure that the yield represents.

Senator Dodd. How about accounts that use variable interest rates?

Mr. Fox. Well, I believe what the legislation calls for in advertisements are simply that if you have tiered interest rates and a particular rate is disclosed, that information associated with that rate needs to also be disclosed, but other tiers need not be disclosed.

VARIABLE INTEREST RATES BECOMING TRICKIER

Variable rates are becoming trickier and trickier. As far as I can tell, there is no such thing on a deposit account other than a certificate of deposit, but on a transaction account there is no such thing as a guaranteed rate any more and virtually every institution will reserve the right to change the interest rate at will.

At one point in developing the legislation a couple of years ago I think there was an attempt to make a distinction between variable rates and fixed rates. I'm not sure that that's very meaningful any more because there seems to be no such thing as a fixed rate.

Senator Dodd. Is that done on deposits? I mean clearly in the housing industry there was an effort made.

Mr. Fox. Well, what you have are not accounts by and large that are tied to an index the way adjustable rate mortgages are. Adjustable rate mortgages are by and large tied to a specific index with a specific margin and so the adjustment is essentially automatic at various intervals.

Senator Dodd. Then maybe we ought to disclose the index yields.

Mr. Fox. Well, unfortunately, with respect to deposit accounts the variable rates are simply set by management from time to time and it would take me a little while to find the page in this same document that discloses that, but essentially the vast majority of commercial banks, I believe well over three-quarters, that have a way of setting deposit account interest rates periodically essentially do it by periodic management decision and not by reference to an index and a margin.

INVESTABLE BALANCE APPROACH

Senator Dodd. You brought up and I brought up the investable balance approach, and I cited that example and you referred to a percentage of banks that are using that approach today. I think you bring up a very good point about in any other area where truth in advertising requires that the consumers know kind of what they're getting.

Do you have any objection, Mr. Shipman, to the comments that have been made about the investable balance approach disclosure?

Mr. Shipman. Only that I really believe that the way to communicate that is paying the principal amount. The statute that we're talking about, if you're disclosing the principal amount that was invested, and I go back, if you have to disclose both yields, it will include every dollar, including that reserve that you're talking about. So it drops the yield in the disclosure to such a deviation when the customer sees that that he's going to ask all the questions that will be again in the bill in the full disclosure and he'll see how it's done.

Senator Dodd. But isn't there something fundamentally unfair about that? I mean you could put it in a bottom line on a disclosure and there seems to be something just inherently wrong about the fact that a person putting in some money should not expect that they would be getting interest on whatever they put in.

Tell me if I'm wrong on that. I'm just having a gut reaction to that account, but why do we allow that?

Mr. SHIPMAN. Mr. Chairman, I really think again the savings account type deposits are not the large dollar amount deposits. With the new deregulations we've had we're talking about money market checking accounts, and the large portion of your consumers are investing in that rather than savings accounts, in CD's and those types of instruments. That disclosure that we're talking about, especially on the checking accounts, would take care of it. By saying principal amount, you have a $10,000 account, then we have to quote the yield on that $10,000, and if you're only dealing with investable balances, that's going to drop so disastrously that I just don't see that that would be a problem.

Senator DODD. Do either Mr. Pitt or you, Mr. Silver, care to comment on this?

Mr. SILVER. Well, this is not quite——

Senator DODD. By the way, is that number going up in the percentage of banks that are using the investable balance approach?

Mr. SHIPMAN. No. I think, if anything, it's going down. With the efforts of the ABA in sending out a lot of disclosure information it has probably been going down.

Senator DODD. Is that your opinion?

Mr. FOX. We never heard of it until this year, and when I first heard of the practice and called people I know at the various regulatory agencies, most of them had never heard of it either.

I got the impression from a couple of the banks where I spoke to customer service people that this is by and large a relatively new practice that in many cases was just initiated earlier this year.

We enclosed an example in the testimony of a bank that attempted to initiate the practice just last month. That bank eventually backed off because of public pressure. But it's my impression that it's a relatively new practice, and if it's being discontinued it's only because of public pressure in the last 3 months.

Senator DODD. Well, that's sometimes better than a law in trying to get things done. It's much more effective and quicker in many ways.

But I would like to know if we could get some percentages if you can from the ABA on how long this has been in practice and if there is any indication. I would like to know whether or not we're seeing an increase in that activity and, if there is, I would be interested in that.

Senator DODD. I'm sorry, Mr. Silver, you were going to comment, and I didn't mean to interrupt you.

Mr. SILVER. I was simply going to comment from my securities perspective. I remember Justice Brandeis once said sunlight is the best disinfectant, and I think that is really the point you just made.

Mr. PITT. As I said in my testimony, we don't, to my knowledge, have any savings institutions that are using that methodology and we think that it needs to be on the full disclosure.

Senator DODD. You, Mr. Fox, have talked about and called for a consistent format for disclosures in other legislation and we have required clear and conspicuous disclosures in the language we've used and that seems to have been working pretty well.

Do you think such a requirement would be adequate here?

FEE SCHEDULES

Mr. Fox. I think the clear and conspicuous disclosure ought to be applied to the various terms that are discussed in the advertising section of the bill. There is another section of the bill that deals with what are called fee schedules where all of the terms of an account would be laid out in greater detail than would be required in an advertisement, and it would be my expectation that in the development of regulations there would be some format guidelines that would set those tables up in a way that consumers would be able to make comparisons because of the use of consistent terminology and consistent formatting.

Senator Dodd. Mr. Shipman, I appreciate the distinction that you've made in your testimony between a depository institution's savings product that guarantees a certain rate or return in the future as opposed to a money market product that contains no such guarantee.

I wonder whether or not you think money market funds should be required to disclose that their yields do not represent any future commitment to pay a specific interest rate?

Mr. Shipman. Well, the mutual funds certainly do not give any guarantee. They work on the past performance of the mutual funds. That's certainly something that I think we are recommending in our testimony that there be some similarity. We need some similarity in the consumer being able to distinguish what the mutual funds are talking about when they quote yields, and generally speaking that yield is not in the future at all and it's no guarantee on the Ginnie Mae's type mutual funds. Those are all on past performance of that fund. I hope I'm directing the answer to what you wanted.

Senator Dodd. Go ahead, Mr. Silver.

Mr. Silver. If I may comment, Mr. Chairman. First, I would like to disentangle two factual matters which have really gotten mixed up here.

There is no present controversy anywhere except at this table with respect to money market fund advertisements. That was settled years ago by the SEC.

Senator Dodd. Well, wait a second. For instance, it's not insured. Do you think consumers ought to know whether or not they could lose money?

Mr. Silver. Certainly. Mr. Chairman, if I may finish my thought.

Senator Dodd. I apologize. Go ahead.

Mr. Silver. Mr. Pitt's testimony, with all due respect, starts off talking about money market funds. Then it switches into an area which is a subject of current controversy, the advertising of long-term bond funds. Now the money market fund formula that the SEC adopted, which is a uniform formula, requires disclosure of the period for which the fund has calculated yield. It's a retrospective 7 day calculation, and that must be disclosed. You can't project the future, and that's why we don't.

The formula which was adopted some years ago and works very well. Also as you know, money market funds invest in instruments that mature in 40, 50, and 60 days.

Senator Dodd. Well, let me ask Mr. Shipman whether or not he thinks that we ought to require that consumers be informed that because money market funds aren't insured that they might lose money? Should they be aware of that?

Mr. Shipman. Yes, very definitely I feel they should be, but moreover on the mutual funds than the money market funds though because that's where the real discrepancy is where there is no predictable yield.

Mr. Silver. Mr. Chairman, now we get to the second point of fact. It is other mutual funds, the long-term bond funds, that are involved in the present rule-making of the SEC and which have engendered sole controversy. Mr. Goelzer can take of himself and I'll let him do that later.

But since January 1986, on a voluntary basis the mutual fund industry has made a full—not footnote—a full textual disclosure with respect to the bond funds, that the principal value will fluctuate. That's in the text. And not only that, but on a voluntary basis all of these ads contain the net asset value, the value per share at the beginning of the last previous year and at the close of the last previous year.

So not only is there a textual disclosure that you can lose money through capital fluctuations, but there is an actual illustration based on the net asset value. Now this is part of the SEC's proposed rules, but the industry has been doing this on a voluntary basis. As Mr. Shipman said, it is those mutual funds in which you take the real risk of loss, not money market funds.

ELECTRONIC MEDIA ADVERTISING

Senator Dodd. Thank you, Mr. Silver, very much.

Mr. Shipman, you of course opposed any disclosure requirements for electronic media expressing your concern about the burden that would place.

I think it's interesting to note, by the way, that one of the examples I cited here, a radio advertisement for the Perpetual Savings Bank product that I indicated earlier did not indicate the minimum balance requirement. The radio advertisement did require a statement of a minimum balance of $2,500. The print did not.

I would be interested to know how that happened. I don't know whether it was a mistake or whatever, but obviously a decision to keep it out. And certainly you're correct in raising the problems that are associated and the greater difficulties with making disclosures, going back to my earlier point to Mr. Fox about how much in the amount of advertising you can get in all the disclosures on, and of course there is no formal application and they're doing that. You're just watching something on TV or listening to it on radio and you're not having something in front of you to sign at that particular moment, and I think that is also a very legitimate point that you make.

Discounting the Claims on Closed-End Mutual Funds

By Jane Bryant Quinn

Closed-end mutual funds are suddenly the darlings of the brokerage biz. After years of hardly rating a mention in the tip sheets, 47 new funds have been sold in the past 19 months and seven or eight more are in the pipeline. Nuveen's $1.5 billion Municipal Value Fund, brought to market in June, was the largest public offering in Wall Street's history.

How long can the romance last? As long as it takes new customers to learn that they're probably buying into a loss. You can find some great plays in older closed-end funds, but buying a new fund is like taking a dip in an alligator swamp. Eventually, you're going to get chomped.

The reason lies in the structure of closed-end funds. Unlike traditional mutual funds, they will not redeem your shares at net asset value (which reflects the current worth of the fund's investments). Instead, their shares trade on a stock exchange, priced according to supply and demand.

When interest is strong, the stock price can run higher than the fund's net asset value. It's then said to be trading at a premium—the ideal state for a closed-end fund, but rarely reached.

More often, closed-end funds trade at a discount, which is something less than net asset value. For example, you could buy $10.08 worth of assets in the Growth Stock Outlook Trust last month for only $8.88—a 12 percent haircut. That fund came out in 1986 at $10 a share, so its first investors lost.

When brokers beat the drums for a new closed-end fund, they're always promising that it will sell for a premium. That's how they get investors to buy. But in fact, the life cycle of a typical closed-end fund runs roughly like this:

- The initial buyers pay 6 to 8 percent more than the fund is worth to cover the broker's underwriting commission. There are no "no-load" (no underwriting commission) closed-end funds. A fund that borrows the money to pay the commission is not a no-load, although some brokers might claim that it is.
- During the first three months, the fund tends to trade at a premium because the issuing brokerages support the price. Gladdened investors break out the champagne.
- After that, the fund is left to find its own level, usually down. Buyers cork up the bubbly and complain to their brokers. The average discount on stock funds brought out in the past two years, and that have passed their three-month birthdays, is 14 percent, says Miami broker Thomas Herzfeld, who specializes in these investments.
- The early money is made by sophisticated traders who sell the new funds short. They're betting that the price will drop, and they're usually right.
- The later money goes to investors who let the fund drop to a substantial discount and then buy in. If its market value rises, so should your shares. With any luck, the discount might rise from, say, 15 percent below net asset value to only 5 percent below. That gives you an even better return.

One fascinating gamble is a trading system developed by Seth C. Anderson, a finance professor at Auburn University in Auburn, Ala. He studied what happens when you let closed-end stock funds drop to various discounts, buy them, then sell when the discounts narrow by a certain amount. Over each of the three time periods he tested, he handily beat the market averages, often by 200 to 300 percent.

His most successful strategy was buying closed-end stock funds when their discount exceeded 20 percent and selling them when the discount narrowed to 15 percent. From 1977 to 1984, that yielded a return of 447 percent, compared with 126 percent for Standard & Poor's 500-stock index.

Why do discounts shrink? Buyers get interested in the fund—because of its performance, yield or some other reason. Discounts widen again when the market goes bad or buyers jump onto some other bandwagon.

The funds of the hour on Wall Street invest not in stocks but in bonds, and they seem to be defying the odds. Instead of selling at discounts, 23 out of 34 are selling at premiums to net asset value. Like the stock flacks before them, the bond flacks say that their new funds won't go to a discount, because investors pay extra for income.

But historically, closed-end bond funds have indeed sold at discounts, Anderson says, although not as large as the discounts on equity funds. Your best strategy on all closed-ends: Buy on deep discounts and hold for better times. ■

#

But don't you think that these ads at least ought to disclose the yield on a standardized basis and indicate if there are certain other conditions that might reduce the yield?

Mr. SHIPMAN. The investable balance method that we are proposing would be protected from any misleading advertising if the APY is also stated. We think that's sufficient in any advertisement on print or the media.

Senator DODD. Mr. Fox, do you have a comment on that?

Mr. FOX. Increasingly we're finding that balance requirements, and I'm not talking about the balance calculation method, but the dollar value of balance requirements are really the most important factor in any account, and I don't see any clear reason why a simple dollar figure is going to clutter up either a print ad or a broadcast ad.

I also heard the radio ad for this particular account in the taxi on the way over this afternoon, and they managed to mention "$2,500." I don't know if anybody held a stop watch to that, but I don't think that took very long to say "$2,500". It's about as long as it takes to say "minimum balance," which is all the print ad discloses.

That's a key factor in the account and is simply something that should not be left out of any advertisement that refers to an interest rate or yield when that's such a material fact.

Senator DODD. How about you, Mr. Pitt, any comment on that?

Mr. PITT. We wholeheartedly agree. As a matter of fact, the balance requirement is already in the Federal Home Loan Bank Board's regulations, and we agree with you. It should be there.

Senator DODD. And what about in electronic media advertising where there is no formal solicitation occurring, although the way they're getting now with cable television you can go buy your groceries and do everything else through cable and maybe you'll be able to have your own little electronic banking system as part of your new TV set or something.

Mr. PITT. It certainly presents a more difficult problem for you in presentation, but we again agree that there is no reason why it shouldn't be disclosed and we have no objection to it being disclosed and in fact think it should be. We don't have any specific methodology as to how it should be done, but we have no problem with it being done.

Senator DODD. I appreciate your comment.

Mr. SILVER. If I may comment, Mr. Chairman, again drawing on my securities law background.

I'm uncomfortable with any wholesale exemption of electronic communications. There is no such exemption in the securities laws. Obviously the regulatory body must draw its regulations to fit the circumstances.

Senator DODD. Well, how much of the securities industry advertises?

Mr. SILVER. Quite a bit. It's growing and the ads are regulated and there are required disclosures. Obviously, as I say, you shouldn't force somebody to take a 30-second ad and make a 90-second ad out of it. Rather than a wholesale exemption, I think there could be recognition given to the nature of the ad. I think the agency should be mandated to adopt such rules as fit the particular circumstances and medium.

I may say that about the bill as a whole, it seems very specific. I think that the important areas certainly should be highlighted, but I think that the agency should be given a good dose of residual authority to prevent any advertising which is fraudulent and misleading and to shape appropriate rules to fit the circumstances of the particular medium or the particular product being advertised.

Senator **Dodd**. I've taken a great deal of your time, all four of you.

In fact, I have additional questions which I'll submit, but I don't encroach upon the time of my good colleague, Senator Karnes from Nebraska who is here.

Do you have any questions at all for this panel?

Senator **Karnes**. Mr. Chairman, no, I don't. I understand from my staff person that all the questions that I had sought responses to had been asked and already answered.

So I appreciate you having the hearing of course, and I apologize for being late, particularly to my good friend, Theo Pitt. I regret not being here for your testimony.

Thank you, Mr. Chairman.

Senator **Dodd**. Thank you.

And again I want to thank all four of you for being patient and waiting.

Again, there may be in addition to the questions I may add, but other members of the committee may have some as well.

We thank you for your candidness and the good points you brought, all of you.

I understand my former colleague from the House—has he arrived, Congressman Lehman?

[No response.]

Well, if not, then I'll go on with Dan Goelzer, the general counsel from the Securities and Exchange Commission.

You've been most patient. The most patient award will go to Congressman Lehman, but he hasn't been here so he doesn't qualify for that. [Laughter.]

Mr. Goelzer, we welcome you here today. You've heard from the Banking Commissioner of Connecticut and a panel of four distinguished witnesses, and I'm going to apply the same admonition to you that I did the others, to try to keep it to 5 minutes.

The full text of your statement I promise you will be made a part of the record, and I'm sure that we'll have some questions for you.

STATEMENT OF DAN GOELZER, GENERAL COUNSEL, SECURITIES AND EXCHANGE COMMISSION

Mr. **Goelzer**. I will try to be brief.

Thank you very much, Chairman Dodd and members of the subcommittee.

My name is Daniel Goelzer, and I'm the general counsel of the Securities and Exchange Commission.

I appreciate the opportunity to be here this afternoon to testify on behalf of the Commission concerning investment company performance advertising.

The bill that the subcommittee is considering, S. 1507, would apply certain uniform disclosure standards with respect to bank deposit interest rate disclosure and fee disclosure.

The Commission does not have any regulatory jurisdiction with respect to the advertising of depository institutions and we have no position on S. 1507 as introduced.

In contrast, however, the Commission does have authority with respect to the advertising and other disclosure of mutual funds. My written statement explains how the Commission has discharged that authority, explains some proposed changes in our rules in that area and explains why the Commission believes that S. 1507 should not be amended to include mutual funds.

I would like to just summarize five points that are discussed in greater detail in my written statement.

First, under the Federal securities laws the Commission has broad authority to regulate investment company disclosure, including advertising. The Securities Act of 1933 requires the filing of a registration statement and a prospectus containing information prescribed by the Commission for every public offering of securities, including offerings by investment companies. The prospectus must be provided to investors who purchase in the offering.

The Securities Act imposes extensive civil liability on issuers, their directors, underwriters and professionals who participate in the offering if there are material misstatements or omissions in the prospectus or registration statement.

In addition to requiring the distribution of the prospectus, the Commission allows investment companies to advertise. That advertising is, however, constrained in several important ways.

Anything contained in the advertisement must also be contained in the statutory prospectus. The advertisement must indicate how a prospectus can be obtained and must caution the investor to read the prospectus before investing. So the ad isn't the selling document. It's simply something directing the investor to the prospectus.

All advertising must be filed with the Commission, and the general antifraud prohibitions in the securities laws, such as rule 10b–5, apply to investment company advertising.

Second, since 1980, the Commission has required that any money market mutual fund that advertises past performance use a standardized method of computing yield. I want to stress that point because one of the earlier witnesses suggested something to the contrary.

Third, in a release issued last fall, the Commission proposed to extend the rules concerning mutual fund performance advertising to all mutual funds. Those funds that choose to advertise past performance under the proposal would be required to use standardized computations. The full text of that proposal is attached to my written statement.

The Commission's Division of Investment Management has received 46 comments on the proposal. The division is in the process of reviewing those comments and it expects to make a recommendation to the Commission sometime this fall.

Fourth, S. 1507 talks about the disclosure of fees and other charges. The Commission already requires that investment company prospectuses disclose all fees and charges. Money market advertisements which include yield must take expenses into account in computing the yield.

The Commission's pending proposal would apply these same requirements to the advertisements of any mutual fund which includes past performance figures.

In addition, at its open meeting tomorrow the Commission will consider another proposal which would require mutual fund prospectuses to present in a table at the beginning of the prospectus all fees and charges so they could be more easily understood by investors.

Fifth, bank advertising concerning promised future returns on deposits and investment company advertising concerning past performance are, in my opinion, completely different and require different regulatory treatment. Securities of investment companies differ functionally from deposit accounts. Bank depositors have an absolute right to the return of the amount deposited, plus promised interest. Mutual funds don't promise a return on capital.

Many funds advertise past performance figures, but the standardization of investment company past performance disclosure raises a host of difficult technical issues which the Commission is grappling with as reflected in our release

These issues include, among other things, as the accounting treatment of fund income and expenses, the impact on yield of amortizing premium or discount on items in the fund's portfolio, the impact of sales load, and the relative importance to investors of the yield on fund assets, the amount actually distributed to shareholders, and total shareholder return.

Disclosure by banks and thrifts concerning promised future yield and deposit accounts does not raise these same issues.

Mr. Chairman, that completes my summary of my statement. I would be pleased to try to answer any questions you may have.

[The complete prepared statement of Dan Goelzer follows:]

STATEMENT OF DANIEL L. GOELZER,
GENERAL COUNSEL, SECURITIES AND EXCHANGE COMMISSION,
BEFORE THE SUBCOMMITTEE ON CONSUMER AFFAIRS OF THE SENATE BANKING,
HOUSING, AND URBAN AFFAIRS COMMITTEE

CONCERNING ADVERTISING BY INVESTMENT COMPANIES

August 5, 1987

Chairman Dodd and Members of the Subcommittee:

I am pleased to testify on the subject of advertising by investment companies under the federal securities laws, in connection with the Subcommittee's consideration of S. 1507, the proposed Truth in Savings Act. That legislation would provide for uniform disclosure of the rates of interest payable on deposit instruments offered by depository institutions, and the fees assessable against such accounts. The Commission generally does not have jurisdiction over the offering of deposit instruments by depository institutions. Accordingly, I express no views on S. 1507 as introduced.

I understand, however, that the Subcommittee may consider whether this legislation should be amended to include investment companies. I believe that such an amendment is not necessary. The Commission has broad statutory authority under the federal securities laws to regulate investment company advertising, and is exercising that authority to assure that investors receive full and fair disclosure concerning, among other things, mutual fund performance and charges. Moreover, securities offered by investment companies differ functionally from deposit accounts of depository institutions. Accordingly, disclosure by investment companies concerning past performance and disclosure by banks and thrifts concerning promised future yield on their deposit accounts require different regulatory treatment.

I. The Regulatory Scheme For Investment Company Advertising

A. Rules Applicable to All Investment Companies

Offerings of securities by investment companies, like offerings of securities by other issuers, are regulated under the Securities Act of 1933. [1] That Act is designed "to provide full and fair

disclosure of the character of securities sold" to the investing public. [2] The Act accomplishes this goal by requiring that a registration statement and prospectus containing adequate and accurate information be filed with the Commission for each public offering of securities. The prospectus must be provided to investors in the offering.

The Act gives the Commission broad authority to prescribe the contents of registration statements and prospectuses. In the case of investment companies, the Commission has required that registration statements and prospectuses disclose, among other things, fees and charges, investment objectives, risks, financial statements, and the background of the investment adviser. [3] The Act also imposes civil liability on issuers, their directors, underwriters, and professionals for material misstatements or omissions in registration statements and prospectuses, subject to certain defenses.

---

[1] Section 3(a) of the Investment Company Act of 1940 defines an "investment company" to include any issuer engaged primarily in the business of investing, reinvesting, or trading in securities. While the Securities Act regulates through disclosure and is applicable to all companies offering securities for sale to the public, the Investment Company Act, applicable only to investment companies, is designed to regulate the actual activities and operations of those companies subject to its provisions. To remedy the abuses of the evolving investment company industry, the Congress in 1940 enacted the Investment Company Act to provide a pervasive regulatory scheme for the detailed control of all aspects of the operations of investment companies. Investment companies register their securities under the Securities Act and register as entities under the Investment Company Act.

(Footnote continued)

1/ (footnote continued)

[2] Preamble to the Securities Act.

[3] To improve prospectus disclosure of expenses, in June 1987, the Commission adopted amendments to Regulation S-X to require to uniform accounting treatment for distribution expenses that are paid out of fund assets. Investment Company Act Rel. No. 15808 (June 12, 1987). In addition, on August 6, 1987, the Commission is scheduled to consider amendments to the registration statements and prospectus form for open-end management investment companies to require tabular presentation of expenses near the front of the prospectus and to require additional narrative disclosure concerning expenses.

The Act requires that written or broadcast communications for the public offer of securities be made by statutory prospectuses, with certain exceptions:

(1) Section 2(10)(a) permits communications preceded or accompanied by a statutory prospectus. This exception allows issuers to send sales literature with or preceded by a statutory prospectus.

(2) Section 2(10)(b) and Rule 134 permit the use of "tombstone ads." These are announcements that simply identify the existence of a public offering and the availability of a prospectus. Investment companies may also provide a general description of the investment company and an attention-getting headline, but may not include any performance figures.

(3) Section 10(b) authorizes the Commission to permit, by rule, the use of communications which omit in part or summarize information in the statutory prospectus.

In 1979, the Commission adopted Rule 482, the "omitting prospectus rule," to permit investment company advertisements to present more information than is allowed in a tombstone advertisement. 4/ Rule 482 was designed to assist investors in evaluating the investment opportunities afforded by funds by permitting funds to disseminate more information in advertisements, including performance data. An investment company can rely on Rule 482 provided that (i) the substance of any information in the advertisement is contained in the statutory prospectus; (ii) the advertisement states from whom a prospectus can be obtained; and (iii) the advertisement cautions the investor to read the prospectus before investing.

Rule 156, also adopted in 1979, 5/ governs the content of sales literature distributed to potential mutual fund purchasers. The Rule emphasizes the general statutory antifraud prohibitions 6/ against using sales literature that is materially misleading in connection with the offer or sale of securities issued by an investment company. Rule 156 also provides general guidance on factors that could make sales literature misleading.

4/ Investment Company Act Rel. No. 10852 (Aug. 31, 1979).

5/ Investment Company Act Rel. No. 10621 (March 8, 1979).

6/ Section 17(a) of the Securities Act and Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 thereunder.

Investment company advertisements and sales literature must be filed with the Commission. The Commission reviews these materials as part of its inspection process for investment companies. All investment company advertisements and sales literature used by broker-dealers that belong to the National Association of Securities Dealers, Inc. must also be submitted to and reviewed by the Association. 7/

B. Advertising by Money Market Funds

The Commission has imposed additional requirements to standardize the yield figures used in money market fund advertising. Money market funds are open-end management investment companies 8/ that generally invest in short-term debt obligations, *i.e.*, money market instruments such as U.S. Treasury bills and notes, certificates of deposit, bankers' acceptances, and commercial paper. Money market funds generally maintain a stable net asset value per share. 9/

In 1980, the Commission amended Rule 482 to require a standardized formula for the calculation of yields of money market funds. At that time, money market funds were experiencing tremendous growth as a result of relatively high prevailing interest rates. The Commission was concerned that the lack of

---

7/ This includes the vast majority of investment company advertisements and sales literature. In its recent advertising proposal, described *infra* pp. 6-10, the Commission has proposed to eliminate the requirement to file advertisements and sales literature with the Commission if such materials are filed with the NASD. These materials would still be reviewed by Commission staff, however, as part of its inspection process.

8/ Section 4(3) of the Investment Company Act defines "management company" to include all investment companies other than "face-amount certificate" companies and unit investment trusts. Section 5(a)(1) of the Act defines "open-end" to describe a type of management investment company which offers for sale redeemable securities. Open-end management investment companies are sometimes referred to herein as "mutual funds" or "funds."

9/ *See* Rule 2a-7 under the Investment Company Act.

comparability of money market fund yield quotations could confuse and mislead investors. Based upon this concern, and the significant role which yield quotations were playing in promoting money market funds, the Commission prescribed a yield formula. 10/

Yield is calculated by dividing the average daily net investment income per share earned by the fund during a seven day period by the fund's average daily price per share over that same period and multiplying the result by 365. In 1983, funds also were permitted to advertise "effective yield" which takes into account the compounding effect of reinvesting fund interest income. 11/ During inspections of money market funds, the Commission staff examines whether yield figures are being correctly calculated.

The Rule also requires that money market funds that charge nonrecurring fees, such as one-time sales or account set-up charges, must disclose in their advertisements that these fees are charged and that they reduce the advertised yield.

Standardizing the yield figures used in money market fund advertising has significantly benefited both investors and the money market fund industry. The Commission's uniform yield standard has enhanced competition among money market funds and enabled investors to compare the performance data of different funds and make more informed investment decisions.

10/ Investment Company Act Rel. No. 11379 (Sept. 30, 1980). Paragraph (d) of Rule 482 provides in pertinent part that:

> In the case of an investment company which holds itself out to be a "money market" fund or has an investment policy calling for investment of at least 80% of its assets in debt securities maturing in 13 months or less, any quotation of such company's yield contained in such advertisement shall be: (1) a quotation of current yield based on the method of computation prescribed in Form N-1, Form N1-A, Form N-3, or Form N-4 and identifying the length of and the date of the last day in the base period used in computing that quotation, or (2) a quotation of current yield described in clause (1) above and a corresponding quotation of effective yield determined in accordance with the instructions as to the calculation of effective yield quotations contained in Forms N-1, N-1A, N-3, or N-4.

11/ Investment Company Act Rel. No. 13658 (Dec. 7, 1983).

C. Proposed Rules Regarding Advertising of Performance Data by Other Open-End Management Investment Companies

The popularity of equity and long-term debt funds has increased in recent years. Assets of non-money market funds grew from $58.4 billion in 1980 to $500 billion by the end of May 1987. While money market fund shareholders outnumbered non-money market fund shareholders during the years 1981 to 1983, 65% of the 46 million shareholder accounts in 1986 were in equity, bond, and income funds, rather than in money market and short-term municipal bond funds. 12/

Fund advertisements frequently include figures indicating their past performance. However, except for money market funds, no uniform method of calculating fund performance exists. Thus, a variety of types of performance data and methods of computing past performance are published by mutual funds. Based upon the success of the standardization of advertised money market yields, the Commission has proposed rules to require the standardization of performance data for open-end management investment companies that are not money market funds. 13/

The release soliciting comments on this proposal states that standardization would enhance the ability of investors to make informed comparisons regarding investments and should promote competition among funds. 14/ However, the proposal would not mandate that funds publish this standardized data. Only funds choosing to advertise performance would be required to use the standardized computations.

12/ Investment Company Institute, 1987 Mutual Fund Fact Book.

13/ Securities Act Rel. No. 6660 (Sept. 17, 1986). Open-end management investment companies, like all other investment companies, are subject to Rules 156 and 482. After the completion of the current rulemaking, the Commission's Division of Investment Management intends to consider whether additional regulations regarding advertising by unit investment trusts would be appropriate. A unit investment trust is an investment company which (A) is organized under a trust indenture, contract of custodianship or agency, or similar instrument, (B) does not have a board of directors, and (C) issues only redeemable securities, each of which represents an undivided interest in a unit of specified securities, but does not include a voting trust. Section 4(2) of the Investment Company Act.

14/ The investment company industry has also recognized the need for uniform standards for income fund performance. In March 1986, the Investment Company Institute, an industry trade association, submitted a proposal to the Commission's

(Footnote continued)

In addition to the standardization of performance figures, the Commission's rulemaking addresses a number of related issues, including proposals to require that disclosures regarding fees and charges be included in advertisements and to improve prospectus 15/ and sales literature 16/ disclosure relating to performance data.

14/ (footnote continued)

staff to standardize yield and distribution quotations of income funds, for funds that advertise performance. The ICI proposal would have prescribed a mandatory, compounded, annualized, thirty day yield and an optional twelve month current return (distribution) figure for funds having the primary investment objective of producing current income through investment in debt obligations. Although the Commission's proposal incorporates certain features of the ICI proposal, there are a number of differences between the two proposals. The Commission's proposal is more comprehensive than the ICI proposal, which generally addresses only issues relating to the standardization of yield and distribution figures advertised by income funds. The Commission did not propose to adopt the ICI proposal as an alternative to its proposal.

The ICI has submitted a comment letter in response to the Commission's release that generally is critical of the aspects of the Commission's proposal that differ from the ICI proposal.

15/ The amendments would require that a mutual fund prospectus contain a brief explanation of the method of calculation and significance of performance data, if the fund advertises performance data. The registration statement filed with the Commission must also present a more detailed explanation of the computation, as well as actual performance figure quotations.

16/ The Commission proposed a new rule under the Investment Company Act of 1940 to apply the standardized performance and disclosure requirements to all investment company sales literature containing performance information. Proposed Rule 34b-1 would deem any sales literature containing performance data to be misleading unless it also includes the appropriate standardized performance data and the legend disclosure proposed to be required in Rule 482 advertisements.

The Commission proposes to extend these requirements to fund sales literature because it believes that the same need for uniformity in Rule 482 advertisements is present with respect to sales literature. However, the proposed rule would

(Footnote continued)

The significant features of the Commission's proposal, which is attached to this testimony, are briefly summarized below.

1. Standardization Of Performance Advertising

The Commission's proposal would limit performance advertising by income funds 17/ to a uniformly computed, thirty day, annualized (but not compounded) yield figure accompanied by a uniformly computed total shareholder return figure covering each of the most recently completed five calendar years and any subsequent interim period. Yield represents fund income as a percentage of the amount invested, while total shareholder return measures all changes in the value of an investment in a fund. The yield figure would be calculated on the basis of prescribed accounting principles. A new fund would present total return quotations for the time the fund was in business. Tax-exempt income funds would be allowed to advertise a tax equivalent yield. Total shareholder return figures generally would be required to reflect all charges deducted from payments to purchase fund shares, all recurring charges assessed against fund assets, and any charges shareholders would bear upon redemption.

Performance advertising in Rule 482 advertisements by all other funds, excluding money market funds, would be limited to uniformly computed total shareholder return figures covering the same periods as prescribed with respect to income funds. 18/ Funds that are neither income nor money market funds would not be permitted to advertise yield.

16/ (footnote continued)

not require the standardized performance data to be the exclusive performance data used in sales literature, since sales literature is not subject to the same space limitations as Rule 482 advertisements. Thus, non-standardized performance data may be accompanied by sufficiently detailed disclosure to explain the data's significance.

17/ The Commission's proposal defines "income fund" as a mutual fund having the principal objective of producing current income primarily through investment in debt obligations and having at least 95% of its net assets invested primarily in debt obligations.

18/ Money market funds would not have to disclose capital fluctuations, since most maintain a relatively stable asset base.

2. Additional Required Disclosure

Mutual fund advertisements containing performance data would be required to include a legend disclosing that the performance quoted represents historical data, and the investment return and principal value of an investment will fluctuate so that investors' shares, when redeemed, may be worth more or less than their original cost. This proposed disclosure will assist prospective investors in distinguishing fund performance claims, which present historical data, and yields or returns on other financial instruments, such as bonds or certificates of deposit. The yield of a fund does not predict future earnings, but instead presents a "snapshot" of recent historical earnings. Similarly, historical total shareholder return does not indicate future shareholder return, but instead presents the past record of a fund. In contrast, the interest on a bond or deposit instrument is contractual and represents the holder's actual future earnings. The recommended disclosures should clarify for prospective investors that fund performance data are historical and that investing in a fund involves both income and principal risk.

In addition, the proposal would require all advertisements to include information concerning sales loads and other charges. If a fund imposes a sales load 19/ or other non-recurring charges, the advertisement must disclose the maximum amount of the load or charge.

3. Equal Prominence Of Performance Quotations

The proposed amendments also would require that multiple performance figures be given equal prominence in fund advertisements. This would require money market funds to give equal prominence to yield and effective yield quotations. Income funds would be required to give equal prominence to yield and total shareholder return quotations. The requirement of equal prominence would prevent a fund from prominently presenting favorable performance data while obscuring less favorable performance data.

4. Stale Performance Data

The Commission also proposed a requirement that advertised performance data be current. Performance data would be required to be calculated as of the most recent practical date, but in no event would the data be allowed to be more than thirty days old.

19/ Generally, sales loads are defined in Section 2(a)(37) of the Investment Company Act as charges deducted from payments for purchase of fund shares.

* * *

The Commission's Division of Investment Management has reviewed the forty-six comment letters received in response to the Commission's proposal and has prepared a summary of those comments. The comment letters raised a large number of complex policy and technical questions that the Division is presently studying. The Division is currently preparing its recommendations to the Commission concerning the proposal and expects to send its recommendations to the Commission this Fall.

II. Functional Differences between Securities of Investment Companies and Deposit Accounts of Depository Institutions

Regulating the advertising and other disclosure practices of investment companies under S. 1507, which is designed to apply to deposit accounts of banks and thrifts, would present practical problems. Although investment companies and depository institutions compete for investors' monies, there are significant legal, practical, and functional distinctions between the investments offered. Securities of investment companies and deposit instruments are not interchangeable products.

A share in an investment company is an equity product: it is common stock upon which dividends are declared and capital gains are distributed only to the extent of the investment company's net income or capital gains. The value of an investor's interest in such a fund necessarily fluctuates as the value of the fund's portfolio of investments rises or falls. A bank deposit instrument is a debt product: it represents a liability of the bank and provides a rate of return in the form of interest. The value of deposits in bank accounts does not fluctuate and, generally, these accounts are insured up to specified amounts. To ensure that investors appreciate these distinctions, the Commission's proposed advertising rules require that fund advertisements using performance data disclose the risk of capital fluctuation.

Because the value of an investor's interest in a fund depends on the value of the portfolio of assets held by the fund, funds do not promise and cannot advertise a future rate of return, as depository institutions do. Many funds do, of course, choose to advertise on the basis of past performance. As described above, the Commission currently regulates such advertising and has proposed additional regulations. In contrast, S. 1507 is designed to ensure adequate disclosure of promised future rates of return on deposit instruments.

Senator **Dodd**. Thank you very, very much.

Mr. Goelzer, I appreciate your being up here today, as I said earlier.

COMPARING S. 1507 WITH EXISTING SEC REGULATIONS

You've obviously had a chance to analyze this bill, S. 1507, that I'm introducing. I wonder if you might share with the committee what the similarities are and the differences between its advertising requirements and those contained in the existing SEC regulations?

Mr. **Goelzer**. Well, I think that in a way is a difficult question to answer because——

Senator **Dodd**. You've seen that list, by the way, that begins on page 2 or 3?

Mr. **Goelzer**. I do have the bill, yes, Senator.

As I mentioned a moment ago, the bill addresses a promise that looks to the future. The Commission's requirements and its proposed requirements address disclosure conserning what has happened in the past. So I think there is a fundamental difference between the objectives of the two proposals.

The bill requires a way of computing yield, and I believe it does it by looking at what you would get on $100 over a certain period of time.

The Commission's rules also require that something called a yield be computed, but again it's based on what the mutual fund actually earned, to what extent its expenses are deducted from that figure, how sales load is taken into account, and other things that wouldn't apply.

The bill talks about minimum balance requirements. I don't think those are particularly an issue in the investment company area, because if an investment company requires a minimum amount to invest and you send in less, they simply won't open an account for you. With a bank I take it they'll open the account, but they'll charge some fee or something that perhaps wouldn't have otherwise have been clear to the investor.

I think the bill calls for a disclosure of a simple interest rate and an effective yield or something to that effect. Again, under our formula you would simply disclose yield and return for various periods. There isn't a nominal rate and an actual rate because the fund isn't promising you anything.

Senator **Dodd**. Well, it's interesting and those are some good points you raised there and are worthwhile noting.

Based on experience and looking at say some States, for instance, that would track more with what we are proposing here and looking at what the SEC has but more retrospective, what is the philosophy, if you will, behind that, and how do they seem to compare in terms of reliability by consumers and in terms of the degree of accuracy in predicting what is likely to happen with their investment?

Mr. **Goelzer**. I'm not particularly aware of any State regulation with respect to mutual fund yield disclosure. I think the problem that we face today at the SEC is outside the money fund area. In the money market fund area, we've already standardized funds advertised yields. Elsewhere, returns are based on a wide range of their conceptions of how they ought to be computed.

I'm not suggesting there is necessarily anything dishonest or unseemly about that. However, there just isn't any uniform guidance that fund can look to, and as a result two identical funds might well disclose two unidentical yields. We are trying to address that problem by standardizing.

Senator DODD. I think you make a good point. I mean again I suppose that for people who make the kinds of investments in mutual funds and the like they are more inclined probably to look on past experience as a way of determining their choices I suppose and that makes some sense to me.

Mr. GOELZER. Well, in a sense past performances is the only alternative in our area because there is no future promise that investor can look to.

Senator DODD. I know, but if you tried to rely on that I think it may be more deceptive. In a sense the past experience is far more reliable prediction for people in that particular area.

You've heard me raise I presume the money market issue, being able to advertise yields based on different time periods which make them hard to compare and hard to assess. I wonder precisely how your proposed rules would deal with that particular problem?

Mr. GOELZER. I would say, Senator, in the money market fund area they are not permitted to have that kind of deviation because, as I believe Mr. Silver indicated, the yield would have to be computed based on our formula over a 7-day period. You would then be required to annualize your return in that 7-day period and the ad would have to indicate the last day of the 7-day computation period.

Outside the money fund area, the area where we don't have rules today, our proposal basically divides funds into two categories, income funds and all other funds. Income funds would be defined as those fund that invest with an objective of obtaining a current return for the investor and have 95 percent or more of their securities in debt, invested in debt. Those funds would be required to disclose the yield that would be computed according to a prescribed formula and would also be required to disclose the total return to shareholders over the past 5 years. Thus you could see not just their current yield, but how an investment in the fund would have gone up or down for each of the last 5 years.

For nonincome funds, that is, all funds other than income funds or money market funds, you would be permitted to disclose only the 5-year total return figures. You couldn't disclose a yield at all. The rationale is that for a fund that's going to have capital gains or losses as a significant part of its portfolio, yield just isn't a meaningful figure. It's total return to the shareholder that's meaningful.

Senator DODD. I appreciate that, Mr. Goelzer. That's very helpful. I've got just a couple of questions on behalf of the staff here.

RULE MAKING PROCESS

They want to know how the rule making process is coming. It's gone on for a year.

Am I doing this right? [Laughter.]

It has been going on for a year and they're anxious to learn how things are and whether or not on the basis of comments you've received that you anticipate any significant changes in the proposed rules and the final product?

Mr. **Goelzer**. It has been going on for a year. I think I would have to say that while I think we would always prefer that we do things faster than we actually do, for something of this magnitude and this level of complexity that isn't an unusual period of time. We did start working from a proposal that the Investment Company Institute gave us, made some modifications to that proposal, and put it out for comment. The staff involved in the area has now summarized those comments and is at the point of formulating recommendations that it will present to the Commission.

They intend that, it come before the Commission sometime this fall, sometime in the next 2 months or so. I'm just not in a position to say to what extent there will be changes between what was proposed and what's recommended to the Commission.

I would refer you again to Mr. Silver's statement that there is at least common ground between the staff proposal and the ICI. We agree that there should be some standardization of the yield computation for funds other than money market funds. So we have common ground in that area, and in other parts of the proposal we do not have common ground.

Senator **Dodd**. That's fair enough, and obviously we have a deep interest in that. That's extremely important in terms of our work product in the time remaining in this session of Congress.

Senator Karnes, any questions?

Senator **Karnes**. Just a couple of questions.

First of all, I would like to hear what comments you've had from consumers, from the constituents and from the purchasers or participants in these funds. Have they been complaining about being misled?

Mr. **Goelzer**. Well, I don't know that I can answer that directly. I did notice an article in Money Magazine which was favorable to our proposal and endorsing it as something that would help mutual fund investors compare funds more easily. I'm just looking at my summary of comments as to whether we had comments from investor groups. I can supply that information for you.

I think we do have complaints generally about the fact that comparability is difficult now because of the fact that there is no uniform and no standardized way of computing return.

Senator **Karnes**. I would be very interested in that information. I find it difficult to follow these computations and calculations on yields and I'm sure the investor does as well.

[The following material was subsequently submitted for the record:]

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

OFFICE OF THE
GENERAL COUNSEL

September 15, 1987

The Honorable Christopher J. Dodd
Chairman
Subcommittee on Consumer Affairs
534 Dirksen Senate Office Building
Washington, D.C. 20510

Dear Chairman Dodd:

During my testimony at the Subcommittee's August 5, 1987 hearing concerning S. 1507, the proposed Truth in Savings Act, Senator Karnes requested certain supplemental information. Specifically, Senator Karnes asked whether the Commission had received any investor comments concerning its proposed mutual fund advertising rules or complaints with respect to mutual fund advertising.

With respect to the Commission's proposed mutual fund advertising rules, the Commission received only one investor comment. That investor generally supported the Commission's proposal. As I mentioned in my testimony, an article in Money Magazine endorsed the Commission's proposal to standardize the method of yield computation used in mutual fund advertisements as an aid that would enable investors to compare funds more easily. (Fried, "How the SEC Would Make it Easier for You to Shop for Government Bond Funds," 15 Money Mag. 43 (Nov. 1986)). A copy of this article is attached for your convenience.

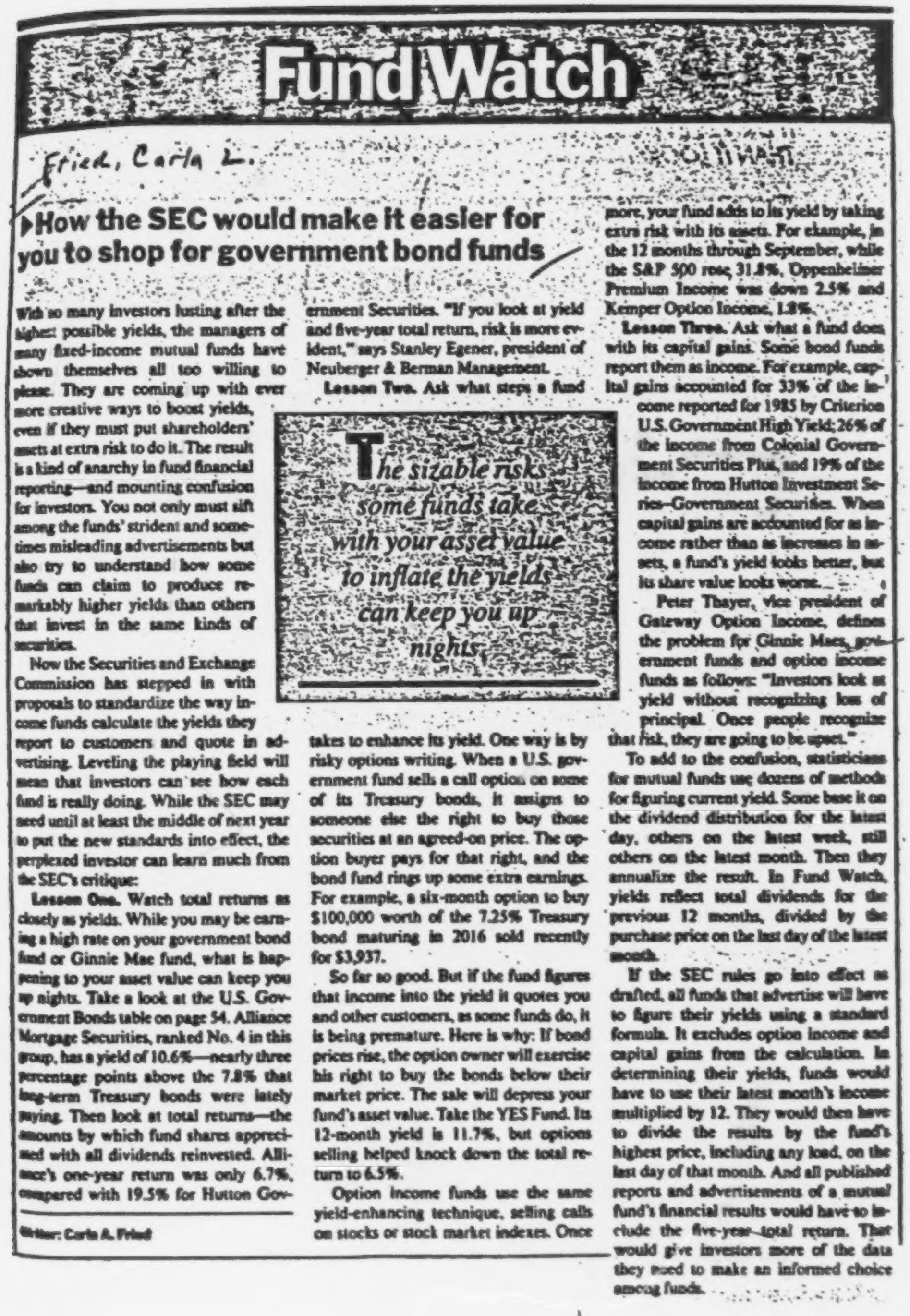
With respect to investor complaints regarding mutual fund advertising and sales practices, the Commission has received an increasing number of complaints in recent years as the number of funds and amount of advertising has increased. The Commission received 53 complaints regarding those issues in fiscal year 1985, 61 complaints in fiscal year 1986, and 123 complaints from the beginning of fiscal year 1987 to the present. In addition, the Commission's Division of Investment Management occasionally receives complaints and suggestions from consumers concerning mutual fund advertising. However, the Division does not maintain records concerning the number of letters it receives or the nature of such correspondence.

If you have any additional questions or if we may be of further assistance, please have your staff contact me at 272-3171 or Barbara B. Hannigan, an attorney on my staff, at 272-2419.

Sincerely,

Daniel L. Goelzer

Daniel L. Goelzer
General Counsel



Fund Watch

Fried, Carla L.

How the SEC would make it easier for you to shop for government bond funds

With so many investors lusting after the highest possible yields, the managers of many fixed-income mutual funds have shown themselves all too willing to please. They are coming up with ever more creative ways to boost yields, even if they must put shareholders' assets at extra risk to do it. The result is a kind of anarchy in fund financial reporting—and mounting confusion for investors. You not only must sift among the funds' strident and sometimes misleading advertisements but also try to understand how some funds can claim to produce remarkably higher yields than others that invest in the same kinds of securities.

Now the Securities and Exchange Commission has stepped in with proposals to standardize the way income funds calculate the yields they report to customers and quote in advertising. Leveling the playing field will mean that investors can see how each fund is really doing. While the SEC may need until at least the middle of next year to put the new standards into effect, the perplexed investor can learn much from the SEC's critique:

Lesson One. Watch total returns as closely as yields. While you may be earning a high rate on your government bond fund or Ginnie Mae fund, what is happening to your asset value can keep you up nights. Take a look at the U.S. Government Bonds table on page 54. Alliance Mortgage Securities, ranked No. 4 in this group, has a yield of 10.6%—nearly three percentage points above the 7.8% that long-term Treasury bonds were lately paying. Then look at total returns—the amounts by which fund shares appreciated with all dividends reinvested. Alliance's one-year return was only 6.7%, compared with 19.5% for Hutton Government Securities. "If you look at yield and five-year total return, risk is more evident," says Stanley Egener, president of Neuberger & Berman Management.

Lesson Two. Ask what steps a fund takes to enhance its yield. One way is by risky options writing. When a U.S. government fund sells a call option on some of its Treasury bonds, it assigns to someone else the right to buy those securities at an agreed-on price. The option buyer pays for that right, and the bond fund rings up some extra earnings. For example, a six-month option to buy $100,000 worth of the 7.25% Treasury bond maturing in 2016 sold recently for $3,937.

The sizable risks some funds take with your asset value to inflate the yields can keep you up nights.

So far so good. But if the fund figures that income into the yield it quotes you and other customers, as some funds do, it is being premature. Here is why: If bond prices rise, the option owner will exercise his right to buy the bonds below their market price. The sale will depress your fund's asset value. Take the YES Fund. Its 12-month yield is 11.7%, but options selling helped knock down the total return to 6.5%.

Option income funds use the same yield-enhancing technique, selling calls on stocks or stock market indexes. Once more, your fund adds to its yield by taking extra risk with its assets. For example, in the 12 months through September, while the S&P 500 rose 31.8%, Oppenheimer Premium Income was down 2.5% and Kemper Option Income, 1.8%.

Lesson Three. Ask what a fund does with its capital gains. Some bond funds report them as income. For example, capital gains accounted for 33% of the income reported for 1985 by Criterion U.S. Government High Yield; 26% of the income from Colonial Government Securities Plus, and 19% of the income from Hutton Investment Series–Government Securities. When capital gains are accounted for as income rather than as increases in assets, a fund's yield looks better, but its share value looks worse.

Peter Thayer, vice president of Gateway Option Income, defines the problem for Ginnie Maes, government funds and option income funds as follows: "Investors look at yield without recognizing loss of principal. Once people recognize that risk, they are going to be upset."

To add to the confusion, statisticians for mutual funds use dozens of methods for figuring current yield. Some base it on the dividend distribution for the latest day, others on the latest week, still others on the latest month. Then they annualize the result. In Fund Watch, yields reflect total dividends for the previous 12 months, divided by the purchase price on the last day of the latest month.

If the SEC rules go into effect as drafted, all funds that advertise will have to figure their yields using a standard formula. It excludes option income and capital gains from the calculation. In determining their yields, funds would have to use their latest month's income multiplied by 12. They would then have to divide the results by the fund's highest price, including any load, on the last day of that month. And all published reports and advertisements of a mutual fund's financial results would have to include the five-year total return. That would give investors more of the data they need to make an informed choice among funds.

Writer: Carla A. Fried

Senator KARNES. I guess the other question I would pose to you, and this is a big theoretical, is we are allowing a number of very innovative products I guess in using some people's terminology to be put in the market. I mean people are being very creative out there as far as the investment vehicles that they are presenting to the public.

My hope would be that there would be some consistency as far as identification of comparable products, and I compliment the chairman for venturing into this very complex area in a very knowledgeable fashion.

But, nonetheless, I want to encourage all the innovation we can in the marketplace and attempt to strike a balance between some of the creating things that are happening that maybe are incorporating some of the new investment tools that we're seeing develop on Wall Street and in other markets with the desire to protect the purchaser and assure understanding.

In your opinion, do you feel that, and I guess maybe I'm answering my own question because the SEC has proposed some rule making in this area, are you concerned that we might by regulating, stifle some of the innovation that we're seeing? We probably don't get a lot of people writing to you I suspect that say these have been great and I've even earned more than I was expecting and I wanted to let you know. I doubt if you get a lot of those types of letters.

It's a bit of a theoretical question, but maybe you could go off in a theoretical bent and respond.

Mr. GOELZER. Well, first, it is true that we don't get too many complaints from people saying that they earned more than they anticipated that they would earn. [Laughter.]

On a philosophical or a theoretical level, it has always seemed to me that one of the strengths of the securities laws and of the SEC is that, as a general matter, all we have to do is require disclosure concerning new products. We don't have to make a judgment as to whether they are sound or unsound. We let the investor in the marketplace make that determination equipped with disclosure about the nature of the product.

It seems to me that the proposals we have in this area are simply an illustration of that strength. We are not trying to regulate the fees that funds charge or the yields that they can pay. We are simply trying to have clear and understandable disclosure for public investor concerning what yields and total return are, so that they can make their own decision.

Senator KARNES. I have no further questions, Mr. Chairman.

Senator DODD. Thank you very much, Senator.

Congressman Lehman has not been able to get over here yet, but certainly his statement will be made part of the record.

And I presume you all know that he was the author of the House bill and has a deep interest in this, and our bill is virtually identical to his that we've introduced.

[The complete prepared statement of Congressman Lehman follows:]

CONGRESSMAN RICHARD H. LEHMAN
STATEMENT BEFORE THE
SENATE BANKING SUBCOMMITTEE ON CONSUMER AFFAIRS
S. 1507 -- TRUTH-IN-SAVINGS ACT OF 1987
AUGUST 5, 1987

Mr. Chairman and distinguished Members of the Committee.

I would like to thank Chairman Dodd for allowing me to testify at today's hearing on S. 1507, the Senate companion to H.R. 176, the "Truth-in-Savings Act of 1987." As lead House sponsor of this legislation, I would also like to acknowledge and thank Senators Dodd, Proxmire, and Heinz for taking the lead in introducing this measure in the Senate and for holding these hearings in such an expeditious manner.

As you all know, I have been actively involved in pursuing truth-in-savings legislation for over three years. Extensive hearings have been held in the House during that time and the provisions included in H.R. 176/S. 1507 reflect that deliberate and thorough legislative process. While not perfect, it is clear that there is broad, bipartisan support for this legislation as noted by the unanimous House approval of truth-in-savings legislation in both this and the previous 99th Congress.

As you well know, our truth-in-savings legislation is a very simple concept that accomplishes three important things. It requires basic and reasonable disclosures in financial institutions' advertising.

Secondly, the legislation provides that certain terms, conditions, and fees be disclosed in statements prior to opening an account, within 10 days after opening an account, or during the life of the account if the yield changes adversely.

Finally, the legislation addresses the so-called "investable balance" issue, a practice in which depository institutions do not calculate the interest on the full amount of funds deposited in that account. This unfortunate practice was brought to the attention of the House Banking Committee at hearings held earlier this year on H.R. 176, and I was joined by House Banking Committee Chairman St Germain in amending the bill to address the problem.

The only unresolved issue is certainly one in which the Senate Banking Committee can remedy. That is the issue of truth-in-savings disclosures as they apply to mutual funds and other similar investment instruments. As you know, this issue posed a germaneness problem for the House Banking Committee, whose jurisdiction is more limited.

Nonetheless, while I generally support the concept of truth-in-savings disclosures for all similar-type investment instruments, I certainly welcome the Senate's assistance in determining whether or not securities-type investment instruments need additional advertising and/or disclosure requirements. Today's hearing should help determine if existing SEC regulations governing mutual funds advertising and disclosure are adequate and comparable to the requirements provided in our truth-in-savings legislation.

Regardless of Senate action in this regard, clearly, in the absence of similar advertising registration requirements and performance rulemaking and standardization among the banking regulatory agencies, some legislative relief to provide uniform and clear disclosure by financial institutions is appropriate.

In summary, our truth-in-savings legislation mandates nothing but clear and uniform disclosure of the yield, rate, and those terms and conditions which can affect the yield on interest-bearing accounts offered by financial institutions. In this increasingly competitive and confusing financial services marketplace, disclosure is the most effective tool and resource which both institutions and consumers can rely on.

As I have stated repeatedly, truth-in-savings is a disclosure concept whose time has come. Again, I appreciate having this opportunity to address the Committee and appreciate the initiative taken by you.

I would be pleased to answer any questions which you might have.

Senator DODD. Your comments here are tremendously helpful.

I'll emphasize again that this rule making process, and I know you still have a ways to go, but to the extent that you can get that done as soon as possible, that will be very helpful to us here as well.

I want to thank all of our witnesses for coming and my colleagues for participating.

The Subcommittee on Consumer Affairs will stand adjourned.

[Whereupon, at 4:12 p.m., the subcommittee adjourned, subject to the call of the Chair.]

[Response to written questions and additional material for the record follow:]

ADDITIONAL MATERIAL SUBMITTED FOR THE RECORD

USL WASHINGTON OFFICE
UNITED STATES LEAGUE of SAVINGS INSTITUTIONS
1709 NEW YORK AVENUE N.W. WASHINGTON D.C. 20006 (202) 637-8930

NEWS

■ RELEASE

WEDNESDAY
AUGUST 5, 1987

CONTACT:	Joan Pinkerton	(202) 637-8930 (office)
		(202) 244-3467 (home)
	James Kendall	(312) 644-3100 (Chicago office)
		(312) 653-4237 (home)
	Allan Friedman	(312) 644-3100 (Chicago office)
		(312) 724-0874 (home)

WASHINGTON, D.C. -- Legislation proposed to give consumers full information about financial products should apply to providers of all types of competing financial instruments, including money market mutual funds, not just federally insured depository institutions, the Vice Chairman of the U.S. League of Savings Institutions testified today.

Theo Pitt, Jr. said the League supports efforts to present interest rate information to the public in clear and understandable terms, even though basic disclosure provisions in the proposed legislation duplicate in large part advertising rules which have long applied to FSLIC-insured institutions.

"We have no objection to codifying those rules," Pitt said.

Pitt, president and CEO of Pioneer Savings Bank, Rocky Mount, N.C., testified for the League before the Senate Banking Subcommittee on Consumer Affairs. The subcommittee is considering S. 1507, a "truth-in-savings" bill already passed by the House.

- more -

Pitt told the subcommittee that the League believes the scope of the House bill is too limited. "It is our strong belief that, in the interest of competitive fairness" the bill should be extended to all financial services providers, including those who sell money market mutual funds, insurance company variable annuities and similar competitors for personal and household savings.

"I have no problem in competing with money funds for the saver's dollar," Pitt said. "But I do have problems competing where the rules of the game favor the money funds, which is precisely what is happening and will continue to happen if those funds are not brought under the provisions of S. 1507."

Pitt said the League welcomes Senate Banking Committee Chairman William Proxmire's recognition that money market funds should be included in the proposed legislation and said "we look to the Senate Banking Committee and its Consumer Affairs Subcommittee to improve this legislation in this regard."

# # #

NATIONAL ASSOCIATION OF FEDERAL CREDIT UNIONS
P.O. Box 3769 Washington, DC 20007
(703) 522-4770

August 5, 1987

The Honorable Christopher J. Dodd
Chairman
Subcommittee on Consumer Affairs
Committee on Banking, Housing,
and Urban Affairs
United States Senate
Washington, D.C. 20510

Dear Mr. Chairman:

I am writing this letter in response to the hearings held today by the Subcommittee on the "Truth in Savings Act" (S. 1507). The National Association of Federal Credit Unions (NAFCU) requests that this letter be included in the hearing record.

When the House Banking Committee was considering similar legislation last year, NAFCU expressed general support for efforts to assist consumers in making meaningful comparisons of interest rates paid by various depository institutions. At that time, however, NAFCU also expressed some reservation with respect to the manner in which that legislation would apply to federal credit unions.

Our concerns, last year, focused on the fundamental differences between federal credit unions and other financial institutions. The "Truth in Savings Act" is directed to the disclosure of interest rates. Earnings on federal credit union accounts, however, are not reflected as interest but as dividends, due to the ownership interest which a member's shares represent. By their nature, dividends are paid after earnings, losses and reserves have been accounted for. Interest, on the other hand, is a contractually agreed upon rate which a financial institution will pay a depositor for the use of that depositor's funds. To require federal credit unions to adopt terminology which is oriented to interest rates and force them to project earnings in a manner similar to institutions which pay interest, ignores the very characteristics that distinguish federal credit union share accounts from the accounts offered by depository institutions. Not only would this practice inappropriately ignore the distinctions between dividends and interest but it would also work to mislead the consumer by attempting to treat accounts on which earnings are

III. Conclusion

I express no view on S. 1507 as introduced. I believe, however, that amendment of S. 1507 to include investment companies is not necessary. The Commission has broad statutory authority to regulate advertising by investment companies. It has exercised that authority to require widespread dissemination of meaningful information to investors and to prohibit fraud in connection with mutual fund prospectuses, advertisements, and sales literature. With respect to money market funds, the Commission has prescribed a uniform method of yield computation. In addition, the Commission has proposed to extend performance advertising standardization to all mutual funds. Because of the Commission's pervasive authority in this area, and because of the inherent functional differences between securities of investment companies and deposit instruments, S. 1507 need not be extended to investment companies.

Appendix: Securities Act Rel. No. 6660 (Sept. 17, 1986)
(proposed advertising rules)

BH/100/(12)cm,jg

a direct reflection of the financial performance of an institution as if those accounts paid a contractually established rate of return.

These concerns were alleviated, last year, by the inclusion of a provision in the "Truth in Savings Act" authorizing the National Credit Union Administration (NCUA) to prescribe regulations within 90 days that are substantially similar to the regulations promulgated under this law by the Federal Reserve Board. The NCUA regulations would govern credit union compliance with this law and would take into account the unique nature of credit unions and the limitations under which credit unions may pay dividends on member accounts. We are pleased that the NCUA authority to regulate credit union compliance with disclosures required under the "Truth in Savings Act" has been included in Section 11 of S. 1507.

The National Association of Federal Credit Unions fully supports the disclosure requirements of S. 1507. Reservations we expressed last year have been eliminated by the inclusion of Section 11 in this bill. NAFCU believes that consumers are entitled to have the benefit of uniform information when comparing the earning potential on various types of savings accounts. As member owned cooperatives, credit unions currently make information regarding earnings on share accounts available to members on a periodic basis and could, with little difficulty, make information on the past performance of share accounts available to new shareholders.

To our knowledge, federal credit union members have little difficulty obtaining information regarding earnings paid on share accounts. As member owned cooperatives credit unions are dedicated to serving the needs of their members. In his testimony before the House Banking Committee on June 4, 1986, National Credit Union Administration Board Chairman Roger Jepsen indicated that the agency has received almost no complaints from credit union members regarding the return on their shares. Such data leads us to question the necessity of including federal credit unions within the scope of this legislation. However, to the extent that the Senate Banking Committee believes consumers will benefit from more complete disclosures regarding earnings on savings, NAFCU supports the approach taken in S. 1507. Furthermore, we believe that as consumers learn more about the characteristics of the interest bearing accounts offered by various financial institutions, they will more fully appreciate the advantages of federal credit union membership.

Mr. Chairman, I would like to emphasize that NAFCU supports the "Truth in Savings Act" as legislation requiring more complete and uniform disclosure of earnings paid on savings accounts. Some have suggested however, that the legislation be expanded to require a specific method of calculating earnings on savings accounts. They advocate requiring financial institutions to adopt an average daily balance calculation method. If such a provision were included in the "Truth in Savings Act", NAFCU would regrettably be forced to withdraw its support.

We have several concerns over adding provisions to this legislation that would require a uniform method of earnings calculation on savings accounts.

At this time, the inclusion of such a provision in this legislation is premature. The "Truth in Savings Act" is intended to address the problems that consumers have in obtaining standardized information about the variety of account options available to them. Without first determining whether this bill eliminates identified abuses in the marketplace, it has been suggested that the Committee consider language that would have severe ramifications on the operations of thousands of credit unions in this country. Before such a drastic step is taken, it would seem more appropriate for the Committee to determine whether increased disclosure requirements provide consumers with sufficient information to choose a savings option that is best suited to their needs.

NAFCU also opposes legislation that would require credit unions to adopt a uniform method for calculating earnings on accounts because such a requirement ignores the traditional characteristics of credit unions. The majority of credit unions in this country are not automated. For this reason, they tend to offer their members a basic savings option, a share account. To this day, many credit unions continue to handpost these accounts. Requiring average daily balance calculation of dividend earnings for most credit unions would overwhelm their bookkeeping capabilities.

Furthermore, credit unions are organized to promote savings and thrift among their membership. To encourage savings, many credit unions have long adhered to the "federal rollback method" of paying dividends on deposits. Under this procedure, deposits made by, for example, the 10th or 15th of a month earn dividends as if those deposits were made on the first day of the month. Deposits after the specified date do not begin earning dividends until the first day of the following month. This type of dividend program encourages members to make regular early deposits into their share accounts by awarding "free" dividends. Credit unions have found this to be a successful incentive for savings among their members.

Individual members are fully aware of the program and value it as a special characteristic of their credit union. If credit unions are required to adhere to a standard form of dividend calculation they will no longer be able to encourage savings by offering their members free dividends.

As legislation requiring specific and uniform disclosure of interest and dividends paid on savings accounts, NAFCU supports the "Truth in Savings Act". If this legislation is amended to require specific methods of calculating dividends and interest, NAFCU would have no recourse but to oppose its application to federal credit unions due to its excessive costs and the adverse impact such a provision would have on traditional credit union operations.

Mr. Chairman, thank you for affording me this opportunity to present the views of the National Association of Federal Credit Unions on this important issue. If you or your staff should have any questions, please do not hesitate to contact NAFCU's Vice President for Government Affairs, Bill Donovan, at 522-4770

Sincerely,

Robert C Hess

Robert A. Hess
Chairman

RAH:cm

○